PRESENT-DAY BANKING IN INDIA

BY THE SAME AUTHOR

ELEMENTARY BANKING

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BY

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To

The Hon'ble SIR ASUTOSH MOOKERJEE,

Kt., C.S.I.,

This book is respectfully dedicated by the

author as a token of his affection,

admiration, respect and

gratitude.

PREFACE TO THE FIRST EDITION.

The Banking Crisis of 1913-15 swept away many of the "mushroom" banks and weakened our banking system to a great extent. Close upon its heels came the War, but it proved a blessing in disguise and the Indian Banking system was improved, reorganised and strengthened to a great extent.

But much remains to be done to perfect our Banking system. With the exception of the leaders of the Co-operative movement our Indian publicists and commercial leaders are not evincing much zeal in the matter.

This little book describes the existing banking system and offers certain suggestions to bring about the much needed improvement in our credit situation. But a soundly organised banking system cannot be established as long as our monetary system is liable to frequent and sudden changes in the value of the different forms of money of which it is composed.

I take this opportunity to express my gratitude to the authorities of the Post-Graduate Department of this University who paid part expenses of my tour which had to be undertaken to study the system of indigenous banking in some of the prominent commercial centres of our country.

banking legislation would tend to make bank management more conservative and enforce legal responsibility for bad management, incapacity, flagrant abuse and peculation. Certainly there are other ways of accomplishing this object. But as long as shareholders elect directors of straw and as long as the present state of public opinion continues to be indifferent the best that could be done is to attempt to cure the evil by legislation. The recent failure of the Alliance Bank of Simla emphasizes the necessity of a more carefully devised legislation and effective supervision so as to enforce responsibility and to guarantee solvency.

SENATE HOUSE :
The 24th April, 1924.

B. RAMACHANDRA RAU.

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PRESENT-DAY BANKING IN INDIA

CHAPTER I.

The Indian Money Market.

"Cash rules the camp, the court and the grove" said Lord Byron and Mr. H. D. MacLeod in his misguided enthusiasm that "Credit is equivalent to cash" would have said that "not cash but credit that rules the camp, the court and the grove." Whatever might have been the opinion of the amatory poet or the enthusiastic economist one finds that credit is the life-blood not only of commerce but in order that agricultural and industrial opportunities may be put to profitable use credit is necessary and that credit can be supplied in a well-developed money market. The money market is the place where the borrowers of money and the lenders of money meet together. A fully organised system of credit can never exist without its indispensable concomitant a well-developed money market. The development of the one leads to the perfection of the other and *vice-versa*.

The Indian money market is generally divided into: (1) the European money market consisting of (*a*) the Imperal Bank of India, (*b*) the European Exchange Banks. (2) The Indian or native money

market consisting of (*a*) the Indian Joint Stock Banks, (*b*) the Shroffs, indigenous bankers and money-lenders. It is these that furnish the needed credit in our money market. The Co-operative Credit Societies have recently arisen and their main mission is to finance the agriculturists and the petty artisans of the towns. The borrowers of money are (1) the Government of India who annually float rupee loans in summer months, (2) the agriculturists, (3) the Entrepreneurs, (4) the Indian people who need money for performing social functions, say, marriages, sraddhas and other functions that have to be performed by people who have a profound faith in the doctrines of karma. The business of the money market is to furnish the needed credit for all these people.

A close survey of the Indian money market discloses the following characteristic features. There is not plenty of loanable money in the market to satisfy all these demands. Secondly, credit has not been thoroughly studied and specialised in all its various forms and manifestations by perfectly organised institutions as in the case of the foreign countries notably Germany and Japan. Credit is generally divided into long term credit and short term credit. Mortgage or long term credit is now undertaken by wealthy individuals and usurious money-lenders much to the chagrin and disadvantage of the borrowers who are being exploited according to the urgency of their needs. Personal or short term credit is given on the strength of the general standing of the borrower or of his surety and it is generally granted for short periods. In the towns

this business is mainly in the hands of Joint Stock Banks and in villages the co-operative credit societies are trying to meet the needs of the cultivators, but to a certain extent the predominance of the usurious money-lender is the third feature of our money market.

Another feature of our money market is that very few systematic attempts are being made to develop the money power of the country by the existing banking institutions. Serious attempts have not been made in the past to induce the people to forsake their hoarding habit and turn their locked up funds into fertile channels of industry and enrich their productive fields. The value of the small account has not been realised by the Indian Banks.*

The lack of a centralised banking institution acting as a "guide, friend, and philosopher" to all the smaller institutions and the consequent lack of concentration of reserves are some of the prominent features of the Indian money market. The creation of the Imperial Bank has remedied this to a certain extent.

The existing credit system is totally lacking in elasticity and any extra demand for currency is not met by the expansion of banking credit. The Indian Banks have no power of issuing notes. Their capacity to create credit in other forms is limited by their cash holdings which they maintain against

* In England a man can open a banking account with five pounds only. The Indian Banks stipulate for a minimum figure of 200 rupees for opening a banking account. They do not pay heed to the relative poverty of the Indian people. Like the American Banks they should be interested in the small savings account and advertise for it extensively.

their demand obligations. A bank's power to create credit is restricted to the extent of its cash reserve. With the small cash balances at the disposal of our banks they cannot aspire to have an undue expansion of credit. The cheque system of issuing credit has not developed to a great extent to amend the inelasticity of the credit media in our country. So there is no easing of the money market to any desirable extent during the busy season.

Systematic attempts should be made to develop the money markets in the lines outlined in the succeeding chapters. A well-organised system of finance should be built up and the oppressive influence and incubus of the money-lender should be eliminated. Credit should be thoroughly organised. It should be made cheap yet not facile. The paralysis of the existing credit system due to the insufficiency of the existing banking institutions should be rectified. All sides of credit, viz., long term credit, short term credit, both for agriculture and industries should be specialised by the existing banks. The habit of thrift should be encouraged. The folly of improvidence should be checkmated. The people should be taught the usefulness of credit and its right use at the right time. Since the economic progress of our country can be facilitated by a perfected credit system alone more attention should be paid to the study of the credit machine in our country. Cheap and easy credit should enable the agriculturist to become prosperous. As Sir Daniel Hamilton says "the present vicious system of finance by the money-lender sterilises the beneficent work of the Government." Real, legitimate

and productive credit should be created to ensure success in commerce, agriculture, and industry.

Many more banks can arise without any detriment to the existing ones. The present Joint Stock Banks are of great value so long as they have plenty of resources and are ably and skilfully managed. The co-operative bank is an essential requisite for every village and more of these wonder-working institutions should be created. Other kinds of banks which provide cheap and effective credit are to be encouraged. They will find their due place in a fully organised credit system of our country.

The saving energy of our people should be stimulated and directed into a broad stream of national finance. The extension of banking facilities or Stock-Exchange and investing agencies of various orders coupled with the ever increasing publicity of the press and of telegraphic facilities for communication of news and transfer of payments may increase the little driblets of savings and turn them into a broad and navigable stream of finance which should be carefully distributed over all parts of our country with increasing rapidity and accuracy of judgment. Our investors should send solid and concrete capital to tap every corner of our country to find natural resources for profitable exploitation.

The main function of our credit institutions is to stimulate and collect the savings of the people, call forth habits of thrift, economy and prudence, guide their outlay into productive channels and stimulate the productive activity of the people. Unless a wisely planned banking system exists developing the money power of our country political

or social reform will be of no avail. As Sir Daniel Hamilton says "without a banking system which will develop the money power of our country the reform scheme or any scheme becomes a dead letter and the new Legislative Council a farce."

A banker is not a mere parasite on the real owners and producers of a country. It is not the business of the banker to augment the capital of the country. Says Adam Smith "all he has to do is to make capital more active and productive than it would otherwise be the case. It is by this means alone that the judicious operations of banking can increase the industry of the country."*

An improved credit system can solve some of the currency ills of our country. The much needed elasticity in our currency system can be obtained. When once the issuing of notes is handed over to the Imperial Bank the note issue will enlarge and as more facilities for their encashment will be provided the notes will become popular and thereby diminish much of the strain on the Government for more metallic currency. Banking extension makes for economy in metallic reserves so far as they are needed for domestic exchange.

A new turn to the banking wheel has been given by the creation of the Imperial Bank. Inaugurating a new era of closer co-operation and greater cohesion among the different banking institutions of our country and arriving at a common understanding of their mutual aims and better realisation of their interests, it should bring about unity where hitherto

* "Wealth of Nations," Edited by McCulloch, p. 257.

discord and jealousy have reigned triumphant. With the cessation of mutual rivalry on the part of the different banking institutions of our country a glorious future awaits all our productive industries and the banks themselves are bound to reap their own share of profit. As they sow, so will they reap.

Some critics contend that a thoroughly organised money market does not exist in India. The upholders of this view point out that the Indian money market is not a separate and a self-sufficient entity by itself. The close dependence on the London money market for funds has been quoted as a proof of its subordination. Isolation, absence of specialisation and differentiation of function still mark our financial organism but like the human organism itself the financial organism reaches its perfection while passing through evolutionary stages and the Indian money market has necessarily to pass through these periods of transformation before it can finally evolve as a perfected and thoroughly organised institution.

"The first and incipient stage is the collection of the credit material. It has to be aggregated into huge masses by the great banks, the savings banks and the co-operative credit societies. The insurance societies have to play "the part of subordinate adjuncts and trustworthy lieutenants" in the process of accumulating money. Money should be tempted out of hoards and thrust into useful activities. The supply of capital should be adjusted to the demand and it should be made mobile and fruitful. This is the duty of our banks and they should try to equalise supply to demand. They should avoid

a plethora of money at one time or a modicum at another.

The second stage of the financial organism is reached when "there is a conscious directing of functions and proper co-ordination of them. It becomes conscious of itself, aware of its own existence, tries to protect itself, to guide and control its own future. It is in this stage that mistakes, miscalculations, reverses and misjudgments may be committed and the financial organism may be put to a trial here but on the whole it endeavours to correct itself and advance on the right path. Then only can the financial organism evolve as a perfected and thoroughly organised whole with proper correlation, interconnection and due juxtaposition of the several elements to each other."*

According to this theory of evolution, the Indian money market is slowly passing through the first stage. There is the accumulation of credit material going on. More banks should arise to mobilise our money power. The various subordinate adjuncts have to perform their mission faithfully and efficiently. The advent of specialisation and the differentiation of functions among the component members of the money market is noticeable to a certain extent but as yet no signs of calculated co-ordination are visible. The present Indian money market may perhaps perfect itself under the intelligent direction of the Imperial Bank during the course of a few years.

* Dr. E. Powell, "Evolution of the London Money Market."

CHAPTER II.

THE IMPERIAL BANK OF INDIA.*

The War has no doubt brought to prominence many economic truths while it has disproved some of the pet theories of economists. It has left us quite a legacy of many difficulties but it has solved many important problems one of which is the vexed problem of the Central Bank for India. From the year 1836 right up to the year 1919 this question has been mooted more than once† but has never been brought to the region of practical politics due to the apathy of the Government of India. But the War brought home to all the parties concerned the utility of a central banking institution with the Government of India having some close relations with it.

Constitution.

The present Imperial Bank of India‡ arose out of an amalgamation of the three Presidency Banks of Bengal, Bombay and Madras.§ The total

* Readers of this chapter should refer to the author's article on the "Imperial Bank Scheme" published in the Indian Review—March, 1921.

† A brief history of the early proposals relating to the establishment of a Central Bank is given in the appendix.

‡ A short history of the Presidency Banks is necessary for a correct understanding of the historical background. Hence their history is included in the appendix.

§ Though the Imperial Bank Act was passed in September, 1920, the Imperial Bank began conducting business on 27th January, 1921.

authorised capital of the bank consists of 225,000 shares of Rs. 500 each. The paid-up capital * consists of 75,000 shares of Rs. 500 each fully paid and 150,000 shares of Rs. 500 each of which Rs. 125 is paid. The Reserve Fund as on 31st December, 1923, was Rs. 4,45,00,000 and the Reserve Liability of shareholders amounted to Rs. 5,62,50,000.

To guard the regional interests and to provide ample freedom in banking matters, the existing local boards of the Presidency Banks have been retained. A central board is created consisting of a general manager or two managers in the first instance, the Controller of Currency (he will be an ex-officio member of the board) and the President and the vice-president of each local board, the Secretary and Treasurer of each local board (these will have no voting power) and four non-official members to be appointed by the Government to represent the tax-payers' interest.† The Central board is created to settle the disputes between the different local boards (if any should arise) to look after the discount policy, to deal with matters of general policy, to determine the distribution of funds, to fix the bank rate and to publish the bank's weekly statements. The central board is to meet once in a quarter of an year at least, alternatively at Bombay and Calcutta but a managing

* The older institutions had an aggregate of 3,75,00,000 rupees of capital and 3,80,00,000 rupees of reserve.

† Representatives of new local boards may be added to the central board. There should be one local board instituted at each of the Clearing House centres—Rangoon, Karachi, Cawnpore, and Lahore.

board is created which will meet more often and transact business. Full provision has been made for the exercising of adequate control by the Government as the Controller of Currency has power to hold up any action of the board on any matter of vital importance affecting either the financial policy of the Government or the safety of its cash balances.

The Imperial Bank has a branch in London to transact such of the business as may be entrusted to it by the Secretary of State for India, to rediscount bills of exchange for the exchange banks, to act as a custodian of the cash balances, and to represent Indian commercial interests in London. It is not allowed to take up general foreign exchange business and compete with the Exchange Banks. While it is granted privilege to borrow money in the London Money Market, on the security of its assets, it is precluded from doing general banking business for all customers except the former ones of the Presidency Banks. It has not been entrusted with the task of floating and managing the sterling loans of the Indian Government as yet.

According to the act the Imperial Bank has to increase its branches by a hundred more within a period of five years and the Government has the option of nominating 25 of them in places of their own choice. At the present time (31st December, 1923) it has 126 branches and three sub-agencies.

The Imperial Bank has been given the free use of the Government reserve treasury funds and the balances of the Government of India and the local

Government. The Imperial Bank manages the public debt work.*

The Imperial Bank transacts the same kind of commercial Banking business which the Presidency Banks performed and some of the restrictions have been modified to a certain extent but their general nature has not been altered so as to permit unsafe business to be conducted. The following are some of the restrictions:—The Imperial Bank shall not make any loan or advance (*a*) for a longer period than six months, (*b*) upon the security of stock or shares of the Bank, (*c*) save in cases of estates (court of wards) upon mortgage or security of immoveable property or documents of title thereof. The amount which may be advanced to any individual or partnership is limited. Discounts cannot be made or advances on personal securities given unless such discounts or advances carry with them the several responsibilities of at least two persons or firms unconnected with each other in general partnership.

The banking business that it can transact is of the following nature†—the receiving of deposits for fixed periods on the payment of a certain rate of

* The following remuneration is sanctioned for this work. A commission of Rs. 2,000 per crore per annum on the amount of the public debt on the books of the public debt offices excluding (*a*) amount of loans discharged outstanding after one year from the date of notice of discharge, (*b*) amount of currency investment, (*c*) amount of stock certificates for five thousand rupees and upwards held by the Controller of Currency, (*d*) the amount of stocks and notes outstanding in the London Register—the Bank is further allowed a fixed sum of Rs. 2,000 a year on account of the stock certificates mentioned in (*c*) above. If the bank manages the debt work of the local Governments the commission is Rs. 3,000 per crore.

† *Vide* Part I of Schedule I of the Imperial Bank of India Act.

interest, the keeping of securities for safe custody, the buying and selling of gold and silver bullion or any other properties that might have come into the bank's possession in satisfaction of claims, the borrowing of money in India or London on the security of its assets, acting as administrator in winding up estates, transacting agency business on commission, the investing of its funds in authorised securities such as trustee securities, securities of Government guaranteed railways, debentures issued by the District Boards and Government securities, the drawing, accepting, selling and discounting, buying and selling bills of exchange—payable outside India for and from or—to such banks as may be approved, the issuing of letters of credit and bank post bills payable in India and Ceylon, and lastly the drawing of bills of exchange and the issuing of letters of credit payable out of India for the use of their private constituents for bona-fide personal needs and buying for the purposes of meeting such bills and bills of exchange payable out of India at any usance not exceeding six months.

Causes for amalgamation.

Though not the first banking amalgamation in our country yet it is the most important one fraught with far-reaching consequences and pregnant with many possibilities. This amalgamation is quite a " spontaneous thing " being the result of a "natural banking evolution in this country." The following are the chief causes that operated in bringing about this amalgamation.

The War has amply demonstrated the weak spots in our banking armour, and the results of a lack of co-ordinated policy on the part of the various banks. Co-operation and co-ordination of policy on the part of the Presidency Banks for a brief period of three years in order to finance the requirements of war have taught them the advantages of such a policy, and the present amalgamation is but a consummation of that desire and they have realised full well that there can be no true and effective co-operation without any formal amalgamation.

Amalgamation is "synonymous with strength" and if the Presidency Banks are to retain the paramount influence which they have so long been wielding, they must combine and if any banking amalgamation of the London Money Market were to obtain footing here the individual and isolated position of three Presidency Banks would mean weakness and inability to compete effectively with such an institution.

India stands in need of more loanable money and the woeful want of banking facilities in the interior of the country is a well-known thing. By this amalgamation additional capital has been secured so as to extend the banking facilities to the interior of the country and promote the healthy development of banking in this country.

Some of the exchange banks are not British concerns. There is a great danger that Japanese and American financial concerns may obtain undue influence and predominance in the monetary affairs of our country if the Presidency Banks remain isolated as before. A close union of Indian and

British interests is necessary for the maintaining of the British Empire, and the amalgamated bank has been given access to the London Money Market to be represented there just like the Dominion Banks of our Empire.

Advantages.

The general public will reap some of the following advantages. There is the popularising of banking business. The opening of branches of this quasi-Government bank with its single and unified management will inspire confidence among the people. It will succeed in inculcating the banking habit gradually and as the Government despatch * says though there may be "no sudden miracle" brought about by the creation of a banking habit yet it is an indispensable preliminary for making people believe in the utility of the banking institutions.

The staffing of the innumerable branches of the Imperial Bank requires men trained in modern methods of banking and this stimulates very considerably the training and employment of Indians as bankers. Thus a banking career † is to be created shortly which may afford relief to the already overcrowded professions of the present day. More of these sound and trained bankers may lead to an improvement in the banking standard of our country.

* *Vide* Government despatch to the Secretary of State for India on the Imperial Bank proposal.

† A carefully constructed apprenticeship scheme has been drawn up and a rapid development of the scheme is necessary in view of the fact that it is increasing its branches.

The advantages to the customers of the Imperial Bank will also be of a weighty character. With the fuller utilisation of the Government balances and a more elastic use of them and with more increased working capital the Imperial Bank can reduce the present high discount rates prevailing during the busy season. A steady uniform and cheapened rate will be the result and it will be a great stimulus to agriculture and commerce in our country. A proper and wise distribution of capital will be another inestimable blessing. The opening of a branch office in London will lead to a closer touch with the London Money Market which is the well-known hub of international commerce. It may lead to the obtaining of trustworthy information regarding concerns in Great Britain interested in Indian trading. Again sterling loans can be arranged for local bodies and investments made in British securities through its branch in London. A largely increased number of branches and the ability to discount more hundies and traders' bills means that the Imperial Bank will be in a position to render yeoman's service in irrigating the channels of internal trade.

The Government of India stands to gain much by the successful working of this bank. Millions of rupees locked up in the reserve treasuries during the busy season usually caused a tightness and stringency in the money market.* The reserve treasuries have been abolished and the Imperial Bank will transform these immense sums of money from mere warehouse

* This can be illustrated from the Bank of Bengal's rates of discount which were altered according to the cash reserves of the Bank and the demand for discount.

merchandise into an active banking power. The Government have undertaken to discontinue the issue of currency transfers to the public between any two places in which a local head office or branch of the Imperial Bank is situated. The Imperial Bank is entitled to transfer its funds through currency free of charge and in return has undertaken to give the public every facility for the transfer of money between the local head office and branches at rates not exceeding a maximum approved by the Controller of Currency.* This means that the Imperial Bank will be responsible for the movement of funds in India and also of making them available to the Government whenever and wherever they are required. This will lead to the opening of more branches and due provision is being made in this direction. The reserve treasuries which hitherto existed acted as a buffer receiving the first shock. Now that they have been abolished the Government's demand would be made

Year	Minimum	Maximum	Year	Minimum	Maximum
1877	7½	14½	1883	7½	10½
1878	5½	11½	1900	3	8
1879	6½	11½	1907	3	9
1880	5½	9½	1910	3	6
1881	5½	10½	1912	3	8
1882	6½	12½			

* The following are the rates approved and these are uniform throughout India and Burma for all telegraphic transfers or drafts issued by the banks.

For sums of Rs. 10,000 and over ...	1 anna per cent.
For sums of Rs. 1,000 and below Rs. 10,000	2 annas per cent.
For sums of Rs. below 1,000 ...	at the discretion of the bank.

Vide Report of the operations of the Controller of Currency for the year 1920-1921, page 32.

on the balances deposited in the hands of the Imperial Bank. This necessitates the keeping of a higher proportion of cash to liabilities than now so as to meet all sudden and large demands but the mere concentration and pooling of reserves will lead to efficiency and economy of the reserves and adequate business accommodation.

The decentralisation of the public debt work hitherto concentrated in the Calcutta Office will improve the administration of the public debt and will encourage small investors of the interior to go in far more frequently for Government securities than is the case now.

The management of the balances of the Secretary of State, his banking and remittance business, if performed by the Imperial Bank's branch office in London would save him a lot of carping criticism by the unenlightened public. As Sir James (now Lord) Meston has said "it would relieve the officers of Government who very often have neither the training nor experience necessary for this sort of work, of obligations and the responsibilities for which they themselves must recognise that they are not fully equipped." It will enable the Government of India to float loans at a low rate of interest during summer months.

The advantages to the Imperial Bank itself are no less marked. It enjoys the proud and privileged position of a bankers' bank. It is bound to become a national institution. Neither a purely European banking institution nor a purely Indian Bank however successfully they may conduct their business have any bright future before them. These can-

never shoulder such immense burden as the extension of banking facilities to the interior of the country. A united stand of both European and Indian people is essential and such a thing is brought about by the Imperial Bank. On account of its immense resources and with Government behind it, the Imperial Bank can successfully play the part of a bankers' bank. It can become a sanctuary to the struggling banks. By virtue of its capital and massive size it will soon obtain controlling influence and be the responsible leader in times of emergency. The successful working of the Imperial Bank will convey to the minds of the people a sense of ease and security hitherto wanting in periods of stress and will make the Imperial Bank a bulwark of public confidence. Access to the London Money Market has been granted and some of the restrictions are relaxed.

The advantages to the Joint Stock Banks have also to be reckoned. The Imperial Bank can guide the banking policy as a whole and be their guide, friend and philosopher. It can rediscount their bills and satisfy their wants for more credit currency. Co-operation and co-ordination of the several banking institutions will lead to better resistance in the time of a crisis and a solid and united front under the leadership of the Imperial Bank will be an effective protection against foreign influences. The Indian banking system will be welded into a co-ordinated whole. It may probably lessen the profits of the other banks holding large reserve deposits but in the security from the operation of the Imperial Bank and in greater stability of business, greater activity and mobility of reserves administered by it the banks

would have protection that would be more than a set off to any diminution of profits.

Coming to the exchange banks it can be confidently predicted that they too will reap their own share in common prosperity. Now that competition in the matter of general exchange business has been eschewed altogether there is no ground for resentment. Their bills will be rediscounted in London thereby enabling them to send back money to India quickly and be in a position to make further purchases of export bills in India.

The co-operative and industrial banks will gain much by the successful working of the Imperial Bank. The duty of rediscounting agricultural and industrial paper will be taken up by this bank and thus it is to act as an apex bank rediscounting paper of the smaller banks. In short it can become the central rediscounting agency. The Government by virtue of its handing over its reserves and balances and entrusting it with the privilege of issuing notes hopes to create a central financial agency looking after commercial, industrial and agricultural interests.

Such are the advantages that promise to flow out of a successful working of the Imperial Bank. But it has to realise its duties. It has to bear in mind that "a central bank is a great note issuing institution in which is vested to an extraordinary degree the financial responsibility of a nation in that, its methods enable it to supply at all times an elastic currency varying automatically with the needs of the country, to maintain an adequate gold reserve through the regulation of foreign exchange and to

conserve and protect the country's metallic reserves to control the money market by its regulation of the discount rate and to serve as a sanctuary for all banks in periods of threatened danger." Such are the functions and onerous duties performed by the national banks of foreign countries. The Imperial Bank should realise that as a national bank it has to keep an eye on national interests. It should not be purely a profit-seeking institution. It should protect and safeguard the general financial situation of this country always. In order to become a central bank it has to make these necessary sacrifices. It should not compete with the other banks. If it were to do so with its far larger resources and special privileges from the Government it would incur their resentment and hostility. It should on the other hand be their refuge in times of panic and trouble.

Hitherto it has been said, that interprovincial jealousies, the large extent of our country and the impossibility of securing capable directors would stand in the way of a central bank. In the present case local boards are given full freedom in their respective spheres while at the same time an effectively controlling central board has been instituted. The question of Government help has been happily solved. But the Controller of Currency* should be alert always and hold up action when the interests of the public are threatened by a misuse of its money. On the other hand he should not make the bank a

* The Government directors of the first bank of Bombay did not realise their duties clearly and this led to its failure in 1866.—*Vide* Sir C. Jackson's Committee's report on the failure of the First Bank of Bombay.

servant of the Government. Independence of the banking power is essential and should be preserved at all costs. As for the fact that competent men will not be found to manage the central bank it must be recognised that "The occasion and the hour always bring forth the man."

THE BALANCE SHEET AS AT 31ST DECEMBER, 1923.

LIABILITIES.	Rs.	As.	P.	Per cent.*
Subscribed Capital	11,25,00,000	0	0	0
Paid-up Capital	5,62,50,000	0	0	5
Reserve	4,45,00,000	0	0	4
Public deposits	8,56,94,171	1	7	8
Other deposits	74,19,50,897	5	9	74
Loans against securities per contra				
Loans from the Government of India under Section 20 of the paper currency Act against inland bills discounted and purchased per contra	8,00,00,000	0	0	8
Contingent liabilities—				
Sundries	38,06,314	4	2	.002
TOTAL ...	1,01,22,01,382	11	6	100.00
ASSETS.				
Government Securities	10,88,70,303	0	4	10
Other authorised do.	1,28,82,071	2	0	1
Loans	21,62,42,156	11	0	21
Cash credits	37,63,94,023	11	4	37
Inland bills discounted ...	11,43,87,342	2	3	11
Foreign bills do.	77,292	14	0	.00007
Bullion—				
Dead stock	2,44,95,084	5	10	2
Liability of constituents per contra...				
Sundries	39,53,334	11	11	.003
Balances with other banks ...	47,65,472	0	10	.004
Cash	15,01,34,302	0	0	15
TOTAL ...	1,01,22,01,382	11	6	100.00

* Rough percentage of total liabilities and assets. The points to be noticed are (1) The large amount of the working Capital that is

Explanation of the Balance Sheet.—On the liabilities side "reserve" relates to the reserve fund of the bank. "Public deposits" are the deposits of the Government for which the bank pays no interest. "Other deposits" are those of the Exchange Banks. Indian Joint Stock Banks, semi-Public Corporations, Traders and private people. These indicate the strength of our banking system. The Imperial Bank does not pay interest on current account but pays interest on fixed deposits on sums not below Rs. 500. "Loans against securities per contra" are usually borrowings of the bank against some of its authorised securities included in the assets side of the Balance Sheet. Loans from the Government of India under Section 19 A of the Paper Currency Act represent sums borrowed on the export bills of exchange or hundies drawn during the course of trading transactions in order to secure easiness of the money market. "Sundries" means miscellaneous liabilities.

Coming to the assets side "Government Securities" mean the bank's investments in Government loans. "Other authorised securities" refer to the holdings permissible under the Act.

obtained by deposits. (2) The loans from the Controller of currency. (3) The magnitude of loans and cash credits. (4) The small amount of foreign bills discounted. (5) The percentage of cash against outstanding liabilities.

The above Balance Sheet includes :—

Deposits in London	738,236	16	4
Advances in London	434,474	3	11
Cash and Balances at other Banks in London	343,117	5	4

Percentage ... 16.4
Bank rate ... 7 per cent.

"Loans and cash credits" refer to the bank's advances to its customers on securities placed in its hands. "Bills discounted" relate to the purchase of hundies and internal trade bills.

"Foreign bills discounted" means the purchase of the foreign bills for its customers only. "Bullion" is the gold or silver held by the bank. "Dead stock" refers to buildings, furniture and movable property owned by the bank. "Balances with other banks" are the accounts opened with other banks to facilitate collection and payment of cheques. "Cash" refers to the amount of cash in hand. This item is important and its proportion against the outside liabilities, viz., the deposits, loans and sundries is expressed as percentage at the foot of the Balance Sheet.

The Imperial Bank finances internal trade to a great extent and some of the big industrial companies are also financed by it. The advances on hundy business are made to the shroffs who in their turn advance money to the outlying places. The Madras branch finances the Natukottai Chetties who finance the Burma rice crop to a large extent. The financing of industries is usually done by (*a*) clean loans which are granted on pronotes signed by two persons and on a personal guarantee of some of the shareholders of the concern. This is how cotton-spinning and jute mills are financed. (*b*) produce loans which are granted on country produce stored in the godowns under the bank's own lock and key. Sometimes the Imperial Bank may discount "hand" bills for approved customers and these are pure finance bills. The Imperial Bank never finances

growing crops except by means of granting clean loans on the personal guarantee of two persons.

Bank Rate.

The bank rate indicates that the Imperial Bank is prepared to lend money on government securities at that rate. The discount rate may be slightly higher than this by one per cent. The discount rate is usually higher in winter and early spring ranging from 6 to 9 per cent., and low in summer say 3 to 5 per cent. On the whole the average rate is not high but it rises to a high maximum during the busy season. When the demand for money is great the rate rises indicating that it is transacting considerable volume of business. During the slack season although the bank rate is nominally low it is willing to lend money at a still lower figure.

The most noticeable feature of the bank rate is that the Imperial Bank does not effectively control the money market just as the Bank of England controls the money market in London. Again the expected lowering, levelling up and equalising of the extremely high rates that prevail for banking accommodation in our country during the busy season has not been realised. The ideally low bank rate of France or Germany or England has not yet been reached.* Of course this is due to the Government borrowings either in the way of short dated treasury bills or permanent loans for longer periods. Unless it ceases borrowing there would not be the possibility

* The average bank rate in 1921 and 1922 was as follows :—

Year	First half	Second half	Yearly average
1921	6.038	5.108	5.573
1922	7.132	4.51	5.81

of collecting surplus cash in the hands of the Imperial Bank of India and a lowering of its bank rate. The seasonal swings* for currency are no doubt responsibile for seasonal fluctuations in the Bank rate, but still the prevailing high rate of discount is chiefly due to the insufficiency of capital in the country.† The uncertain political situation is also a bar to the free export of capital from the United Kingdom to India.

During a short career of two and half years it has displayed promising signs of its alertness and usefulness to the community. The seasonal expansion of emergency paper currency to the extent of 12 crores on export bills of exchange which has been sanctioned by the paper currency act of 1923, has been brought about by the Imperial Bank during this busy season (January to March, 1924). Opening its branches in the interior of the country it is slowly expanding its field of usefulness, and is bringing within easy reach of all sound banking facilities.‡ Its help to the creditors of the Alliance Bank of Simla§ at the request of the Government of India

* During the marriage season, holiday season and holy season there is a great demand for currency.

† This will be discussed at length in the last chapter on banking reform.

‡ It has opened about 59 branches during the course of the two years. The Government of India helped the bank by permitting it to make use of the existing treasury accommodation and strong rooms when suitable premises were not available.

§ When the Alliance Bank of Simla was closed there was a run on the Tata Industrial Bank and the Bengal National Bank. But the Imperial Bank promptly assisted them. *Vide* Mr. B. Chakraverty's speech at the annual shareholders' meeting of the Bengal National Bank held in 1923.

betokens much. It exercised an "imperial outlook" and had a wide latitude of vision when it promised to set its house in order but the evils were too deep-rooted to be remedied. Since the liquidation of the Alliance Bank of Simla the Imperial Bank has been trying to cover some of the abandoned ground. It enabled the Government of India to make huge remittances to London without seriously disturbing the exchange market and the Indian Currency system.* Merchants and traders are making increasing use of the improved facilities for internal remittance. Before long a day may arrive when there will be no charge made for internal remittance through the agency of the Imperial Bank.

Suggestions.

It should bear in mind the following suggestions and carry them out as far as they are practicable. Acting as the depository of the cash reserve of the other banks, performing more business with the banks than with the outside public, thus justifying in reality the term banker's bank relaxing her loaning policy to some extent, realising that it is the handmaid of trade and industry of our country whose imperative duty is to fulfil its ever-changing requirements, caring less for profits than is the case at present, developing to a certain extent the newly permitted acceptance business, organising a discount

* The London Times says "without the remittances made this year the Government of India can pay its way abroad without coming into the exchange market for two years." It says that more rapid development of branch banking is necessary. It recommends the formation of the provincial loans fund to obviate excessive competition between the provinces.—February 4th, 1924.

market and rendering help to all sound banks in their occasional hours of distress, the Imperial Bank can obtain real control in the money market, and uninfluenced by political currents or other members of the banking community it should conduct the whole machinery of banking in the wider national interests of our society. A centralised system under the watchful guidance of the Imperial Bank is an effective safe-guard against an internal panic.

Though the irreconcilable elements, Government control and private management, have been successfully fused as in the case of the American Federal Reserve System, yet the Central Board of the Imperial Bank has no such extensive powers granted to it as in the matter of the Federal Reserve Board.* The two serious limitations, lack of control over the issue of paper currency and lack of power to deal in general foreign exchange business are restricting the scope of its usefulness. If once it loans up to its full limit during the busy season it has no power to expand the currency beyond the 12 crore limit. Hence the bank rate is still soaring to the height of 9 per cent. If there were to be a genuine trade revival and the purchasing power of the continental countries really improves the consequent trade expansion in our country would necessitate a higher bank rate.

The Federal Advisory Council can be copied here with some advantage. The exchange banks, the Indian Joint Stock Banks, the Agricultural and

*The Federal Reserve Board supervises the Federal Reserve Banks, regulates the note issue and defines the bills of exchange that can be discounted.

Industrial banks and the shroffs can be represented in a council which should meet occasionally and exchange its views with that of the Imperial Bank. Such a step would enable the Imperial Bank to feel the pulse of the market and the policy of the Imperial Bank might be changed to their mutual advantage. The absence of a banker's association which can watch the banking policy of the country is keenly felt. The institution of an advisory council is the nearest possible approximation to such an association and hence it should be created as early as possible.

The Imperial Bank should try to bring about direct relation between the Indian money market and the London money market. At present there is only an indirect relation existing between the two. The Indian demand for gold affects discount rates which in turn affects the exchange rates. The Government of India usually loans out a part of its cash balances in the London money market for short periods. These loans weaken the controlling position of the Bank of England and it is not able to pull in gold from India just as she does from other commercial centres by raising her bank rate. The successful working of the Imperial Bank will lead to the lowering of the present high bank rates in India and this may enable the Bank of England to pull in gold from India as well. Thus the Imperial Bank is bound to exercise a marked and perceptible influence on the ebb and flow of gold from India and into India. Then perhaps it will be possible to revise the time-honoured dictum that "India is a sink of precious metals."

Sir M. Hailey invoked the glorious vision of a great State Bank subserving the interests of the

public and rendering equally meritorious service to the other banks doing business in the money market. The Imperial Bank is only a state bank in the narrowest possible meaning of the term. While the balances of the state are handed over to the Bank, for which it clearly gains about two crores on the score of interest alone, the state does not participate in the profits of the institution. A large part of the working capital of the bank is due to the cash balances of the state. Beyond imposing certain restrictions, it does not interfere in the policy of the bank. Perhaps this is meant only as a half-way stage* and at the next revision of the agreement in 1930 more welcome changes may be noticed. No opportunity should be lost to make it a primarily self-sacrificing instrument of an ambitious national programme.

*It is not a genuine central bank as yet. It is a commercial bank masquerading as a central bank. Unless it cheapens credit it would not command due respect and support from the hands of the public.

CHAPTER III.

THE EXCHANGE BANKS.

The official definition of an "Exchange Bank" points out that the head office of the bank should be outside India. The fact that the Presidency Banks were not allowed to deal in foreign exchange business gave scope for these banks to specialise in it. No rigid partition of business exists between the three kinds of banks doing business in India, *viz.*, The Imperial Bank, The Exchange Banks, The Indian Joint Stock Banks. The exchange banks besides dealing in foreign exchange conduct ordinary banking business, *i.e.*, they lend money at call, investment and grant loans but during the busy season, that is, December to March, they invest a considerable portion of their funds in discounting foreign trade bills. It is this special feature that differentiates the exchange banks from the other banking institutions of this country.

The exchange banks fall into two groups. Group 1, Banks whose business in India is limited and forms say 1/10 of the total volume of their business. The following banks belong to this category.

	Name of the Bank.	Head Office.
1.	The Comptoir National D'Escompt de Paris ...	Paris
2.	,, Yokohama Specie Bank	Tokio
3.	,, Somotino Bank	,,
4.	,, Bank of Taiwan	,,
5.	,, International Banking Corporation ...	New York

	Name of the Bank.	Head Office.
6.	The Nederlandsch Indische Handels Bank ...	Holland
7.	,, Nederlandsch Handel Maatschappy ...	,,
8.	,, Hongkong and Shanghai Banking Corporation	London
9.	,, National Bank of South Africa ...	Cape Town
10.	,, Imperial Bank of Persia	Tehran
11.	,, Banco Nacionale Ultramarino ...	Lisbon
12.	,, Llyod's Bank (amalgamated with the Cox and Co. and King Hamilton and Co.) ...	London

Both the Russo-Asiatic Bank and the Deutsche Asiatische Bank have closed their doors since the outbreak of the late war.

Group 2. The exchange banks that belong to this category are the following. Though their head office is situated outside India they have their volume of business conducted mainly in India.

	Name of the Bank.	Year of Establishment.
1.	The Chartered Bank of India, Australia and China*	1853
2.	The National Bank of India† ...	1863
3.	The Mercantile Bank of India ...	1893
4.	The Eastern Bank of India ...	1910
5.	The P. and O. Banking Corporation ...	1921

The newly started Imperial Bank does exchange business for its customers. The Alliance Bank of Simla‡ and the Tata Industrial Bank§ did exchange business on a large scale. One or two Indian

*This bank does no business in Australia. Owing to the hostility of the Press in Sydney it had to give up its attempts of opening an office in Australia.

†It transacts a large volume of business in South Africa and British East Africa.

‡The Alliance Bank of Simla is now under liquidation.

§The Tata Industrial Bank recently amalgamated with the Central Bank of India.

Banks* have recently been started in Bombay to deal with exchange business.

TABLE RELATING TO BANKING BUSINESS.†
£ (1,000) Omitted.

	No. of Banks.	Paid-up Capital.	Reserve.	DEPOSITS In India	DEPOSITS Out of India.	CASH BALANCES In India.	CASH BALANCES Out of India.
Group I (Agencies of large banks doing business in India).	13	58,841	36,638	177,802	455,626	57,832	70,013
Group II.	5	7,000	9,047	556,042	71,722	103,931	11,641

Explanation.—The Exchange Banks are more or less Janus-headed. They perform their business in India and in the country of their origin. They pay a slightly higher rate for deposits than that of the London Joint Stock Banks and pay two per cent. on current accounts provided they do not fall below a stipulated minimum. In India they pay a slightly lower rate than the Indian Joint Stock Banks but their rates are more favourable than the Imperial Bank rates. Formerly they used to take pride in the fact that they obtained capital for India from London but now they have discovered that money can be tapped in India as well. Mr. Keynes wrote that these exchange banks never kept an appreciable cash reserve in India but their position has been

* The Union Bank of Bombay and The Industrial and Exchange Bank. Of these The Union Bank is now under the management of The Central Bank of India and in the near future there may be a complete amalgamation. The Industrial and Exchange Bank has suspended payment.

† This table refers to the exchange banks doing business during the year 1921-1922. *Vide* "Statistical Tables relating to Banks in India," Ninth Issue.

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much strengthened ever since that time. As they perform their business in several places they have to so carefully adjust their resources that they do not suffer from want of capital in any place and this is no easy task. Their position would be very difficult if a concurrent crisis both in the London Money Market and in India were to develop at the same time. Normally they depend on importing funds from London to India and remit it back after the period of employment.

The nature of their business.—The Exchange Banks besides dealing in foreign exchange, *i.e.*, buying export and import bills conduct ordinary banking business competing to a certain extent with the Imperial Bank and the Indian Joint Stock Banks in the matter of loans and overdrafts. They finance internal trade in certain places like Amritsar, Srinagar, and Mandalay. The piece goods trade in Delhi and Amritsar and the leather trade of Cawnpore are financed to a great extent by them. They compete with the Bengal Branch of the Imperial Bank in the matter of financing jute operations. In the Madras Presidency they confine their business solely to the financing of export and import business but they practically do very little or hardly any local business for Indians. They have 46 branches in the interior of the country and there is no statutory restriction compelling them to keep a high proportion of cash reserves as against their liabilities. They deposit a part of their funds in the Imperial Bank of India.

Coming to their exchange business, the export bills are classified as D/A (documents on acceptance)

and D/P (documents on payment). They are bought *in* India by the branches of the exchange banks. These bills are negotiated in India and drawn on London and as they are drawn on well-known houses in London they can be discounted easily. The head office of the bank in London holds the D/P bills till maturity and cashes them. The D/A bills are rediscounted immediately after acceptance at the London Joint Stock Banks or bill brokers or the Bank of England according to the ease or tightness of the money market in London. These bills are usually drawn for three months. They are either "clean" or "documentary." Whether the D/A bills will be immediately rediscounted or not depends on three factors : the nature of the drawer of the bill, the Bank of England's rate of discount, and their own need for cash. If they do not stand in urgent need for funds in India they do not rediscount them. The money to finance the export trade (by means of rediscounting export bills) is British capital and not Indian money.* This is considered a danger to our export trade. As the Indian deposits of these exchange banks increase this danger will be removed. Again the branch of the Imperial Bank in London would absorb much of this rediscount business in future, hence it would be Indian money that will finance our trade.

*No accurate statistical information has been collected with the object of estimating the amount of funds employed in rediscounting the Indian trade bills. Some idea can be had if the amount of the bills rediscounted by the exchange banks belonging to group II is taken into account. It is true that they discount other countries' trade bills also but the Indian trade bills form the major portion of their "bills discounted" item.

The import bills are negotiated *in* London and drawn on India. Again it is the London office that finances the import trade through their London office and its funds there. The bills are drawn D/P or D/A bills in sterling and paid with interest from the dates of the bills to the approximate arrival in London by demand drafts on London. These bills are never rediscounted.''* India is a creditor country† and her export trade is far larger than her import trade and the balance of trade in her favour has to be paid to her and the exchange banks liquidate the balance by buying council bills and telegraphic transfers. They send gold bullion, coin, and silver bullion. Besides this there is the transfer of Government rupee paper from London to India. They buy the sale of drafts required for Indian travellers and students in England. Thus the purchase of export bills is done with the aid of (1) import bills, (2) council bills and telegraphic transfers, (3) gold and silver bullion, (4) transfer of rupee paper, (5) sale of drafts and telegraphic transfers payable in London and elsewhere out of India.

The action of the exchange banks has to be noticed in the matter of the sale of council bills. If money is not forthcoming to rediscount their D/A export bills, the exchange banks have to depend on their own resources. They have to buy export bills and have to transfer for that purpose funds from London to India and this they do by the mechanism

*Banking blue book (business of the exchange banks).

†Economists say that India is a debtor country and in order to pay her obligations abroad she is forced to maintain a favourable trade balance.

of the council bills. Hence a high discount rate in England will slacken the demand for council bills, or again when Indian produce is withheld by speculators to realise higher prices the demand for council bills falls to a low figure.

The exchange banks are doing quite a lucrative business and the eastern exchange banks so far as their dividend is concerned and as the high value of their shares on the stock exchange indicates are thriving concerns and thanks to the gold exchange standard system, the speculative element in their business has been removed and a satisfactory "par of exchange" is established between the silver-using countries and the gold-standard ones. They have passed through a keen struggle for existence. They have obtained great reputation consequent to their long establishment in this country and they are very jealous of any intruders who may encroach on their business. It is the prevailing opinion that it is practically impossible to start a new exchange bank in teeth of the opposition of the old ones. The nature of the business is such that the customers flock to the old exchange banks rather than patronise the new ones.* As Mr. Wolfe observes, "The English banks have subdivided the export field in businesslike fashion, honeycombing each section with branches, agencies and correspondents and through the undisputed position which London has as the centre of financial transactions in internationa.

* Mr. J. M. Keynes says, "Indian exchange banking is no business for speculative or enterprising outsiders and the large profits which it earns are protected by established and not easily assailable advantages."—Indian Currency and Finance, p. 208.

business are very well placed to serve their clients and English export trade cannot help but derive the utmost advantage therefrom." *

Defects.

The exchange banks have protested against the proposal that the Presidency banks should be allowed to do exchange business and have access to the London Money Market. They were against the closing of the mints in 1892. They were against the formation of a central bank for India and viewed with jealousy the proposals for the establishment of a State Bank. They have unfortunately reproduced the same unscientific method of quoting exchange rates as in the case of the London Money Market.

There are two methods employed in our daily quotation of exchange rates. The first method is to state rupees in terms of foreign currency as in the case of New York, Hong Kong, Shanghai, Singapore and Japan. Here the number of rupees against hundred units of foreign currency is stated. According to the other methods of quotation, foreign currency is quoted in terms of rupees. Here there are some anomalies. In some cases as in London and Melborne exchange rates the amount shown is equivalent to one rupee. In the case of France and Germany the Exchange rates relate to the amount of foreign currency against hundred rupees.

EXCHANGE RATES ON APRIL 1st, 1924.

			s.	d.
Telegraphic Transfer	...	...	1	4 11/32
On demand	...	...	1	4 11/16

* Mr. A. J. Wolfe—Foreign Credit.

	Banks selling O/D.	Banks buying 30 D/St.
France	520	...
America	386	...
Hong Kong	174	165
Shanghai	240	227
Singapore	170	164
Japan	141	135¼
Java	83—3/8	86

As there is a difference in the method of quotations such general statements as " buy high " and " sell low " and a " falling exchange acts as a stimulus to export trade " are to be cautiously interpreted carefully noting the method of quotation employed.

It is high time to reduce these quotations to a uniform standard as America has done. Mr. Minty writes, " exchange rates were formerly quoted in America as they are still in England, some so many dollars to the foreign unit and others for many foreign units to the dollar. It has now become the universal practice to quote exchange rates so many cents to the foreign unit or if a finer quotation is required so many dollars and cents to the hundred foreign units." *

In spite of these apparent defects on their part, they have done yeoman service to our country in popularising banking business in our country. Though in the beginning of their career they could not attract huge deposits in India, of late a change has come over the situation. During the last few years their deposits in India have increased

* *Vide* L. M. Minty—" American Banking Methods," p. 302.

considerably.* So long as they are worked by the foreigners (both in the Directorate and staff) they cannot cultivate sympathetic relations with the Indian customers. There is vast and unlimited scope for the Indian Joint Stock Banks to take up the financing of inland trade and the foreign banks can never wholly succeed in monopolising this kind of business as they have done in the field of foreign trade.

The Eastern Exchange Banks have started an Association in order to protect their common interests and they have seldom failed in the past to exert their united strength to protect their interests.

During the War period in spite of a rising exchange and their limited financial resources "they heartily co-operated with the Government in the matter of financing the essential exports required for the war purposes and the market rate of exchange was maintained near the rate at which council drafts were sold."† Encouraged by the Secretary of State's promise they bought export bills far in excess of purchases of exchange in the other direction.‡

When the price of silver began to rise the sale of council drafts could not be made at the old rate without loss to the Government. Any undervaluing of the rupee might tend to make it disappear and so

* The following table shows the deposits attracted in India :—
(In lakhs of rupees).

Year	1895	1900	1905	1910	1915	1918	1919	1920	1921	1922
Amount	1,030	1,050	1,704	2,479	3,354	6,185	7,485	7,480	7,519	7,338

† *Vide* Sir H. Babington Smith's Committee-Report.

‡ "The Secretary of State insured them against the risk of a rise in exchange by undertaking to sell to them within a year after the War, exchange up to the amount of their overbuying at the rate at which their excess purchases had been made."

the exchange value of the rupee was made to follow the price of silver. From 28th August 1917, the rates were changed as follows.* The short-lived attempt on the part of the Government to maintain the official rate of exchange at 2*s*. led to further disorganisation of the exchange situation.†

Such rapid alterations in the exchange value of the rupee made the Exchange banks rather cautious in their "forward" operations of exchange. As Mr. Keynes says " a 'forward' contract is for the conclusion of a 'spot' transaction in exchanges at a later date fixed on the basis of the 'spot' rate prevailing at the original date. Pending the date of maturity of the forward contract no cash need pass (a security as proof of ability to complete the contract is always taken by the Indian Exchange Banks) and he is protected from the consequences of any fluctuations in the exchanges in the meantime."‡ By this method of dealing the importer merchant and the exporter try to eliminate their risks. The

* Date of Introduction		Minimum rate for immediate T. T	
		s.	*d.*
3rd January	1917	1	$4\frac{3}{4}$
28th August	1917	1	5
12th April	1918	1	6
13th May	1919	1	8
12th August	1919	1	10
15th September	1919	2	0
2nd November	1919	2	2
12th December	1919	2	4
2nd Febuary	1920 (2*s*.Gold)	2	$8\frac{1}{2}$ (sterling).

† For a detailed account of the Indian situation the readers should consult the author's article in the Calcutta Review for February, 1922.

‡ Keynes " Tract on Monetary Reform."

Exchange Banker, while undertaking to bear these risks due to fluctuations in exchange protects himself by setting off one operation against the other. He "covers" himself by setting off a sale by a purchase or *vice versa*.

While it is the duty of the Exchange Banker to buy as many export bills as are offered and protect himself as best he can, our Exchange Banks, as soon as they find the free market in exchange breaking down, would insist on the providing of full "cover" for their purchases of export bills. The Exchange Banks then refuse to operate except in 'doubles.' They sell remittances only against bills. Such measures generally cause inconvenience to export trade. This unfortunate situation can only be remedied if "a Central Bank were to quote rates for forward exchange in terms of spot exchange. By varying these rates they would be able to vary the interests offered for foreign balances, as a policy distant from whatever might be their bank rate policy for the purpose of governing the interests obtainable on home balances."* Then it would be possible to mitigate the evil consequences of exchange fluctuations by organising facilities for forward dealings.

This plan is evidently meant for gold standard countries which are anxious to have a control over the fluctuations of the exchange values of their currencies. In India the Government by virtue of

* Mr. Keynes discusses a practical scheme whereby the Bank of England should regulate the value of gold by buying and selling it at a price every Thursday morning. This would keep the dollar sterling exchange steady.

their gold exchange standard system fixes the exchange value of the rupee and its reserve in foreign currency is the gold standard reserve kept in London. When there is an effective gold exchange standard system and when there is a free market in exchange the merchants naturally do not go in for these forward contracts. India being an agricultural country has seasonal exports and during this time the exchange banks' purchase of export bills would be greater and it would be difficult to " marry " the forward purchases with forward sales. The sterling balances would be increased and as soon as their export season is over this position is reversed. The exchange banks sometimes transfer funds to the Indian Money Market to lend them at a favourable rate. Suppose that a nine to ten per cent. rate is prevailing in the Indian Money Market during the busy season while only a three per cent. rate can be obtained on the use of funds in the London Money Market. The exchange banker sells his sterling resources to the importers and cover this by a forward purchase to be taken up three months hence by the exporters. This operation is known as a " Budlee " operation. Even granting that no direct profit has been obtained in exchange, the banker obtains the use of money in India at a favourable rate. When there is " a superfluity of local resources " the Indian Exchange Banks make similar operations in which a ready purchase may be covered by a forward sale.

The exchange banks being few in number and with their close-knit organisation they succeed in obtaining more than competitive profits. Taking the Paris rates of to-day (March 12, 1924) which is

francs 740, it can be proved that they are selling very low in order to protect themselves as it is at present subject to fluctuations. By the chain rule method this statement can be verified.

How many francs	=	Rs. 100
Re. 1 ...	=	1s. $4\frac{11}{16}$ *d.* or $\frac{267}{16}$ *d.* (Banks' selling rate for demand bills).
240*d.* ...	=	£1.
1 £ ..	=	11,840 francs (quotation of exchange on London at Paris).

Hence the required number of francs=

$$\frac{100 \times 267 \times 11840}{100 \times 240 \times 16}$$

$$= 823{\cdot}25 \text{ francs.}$$

Vested Interests.

The attempt of the exchange banks to perpetuate their new monopoly will never succeed. Although they have once again succeeded in confining the exchange business of the Imperial Bank of India solely to its own customers, yet it is doubtful whether their monopolistic position will always prevail. Foreign exchange business is a paying one. As the resources of the Indian Joint Stock Banks increase the struggle for profits would become keen and there would be an effective challenge and real competition with the exchange banks. The newly arising national spirit prompts the people to retain these profits within the country. The desire to retain the natural surplus from our foreign trade* so that our

* Indian economists point out that our foreign trade is wholly financed by the foreign banks and this annual tribute depends on the amount of trade that is financed by them. Our trade figures are estimated at Rs. 500 to 600 crores. Taking the lower figure as the basis of our computation and supposing that the average bank rate is 4 per cent. on an average usuance of three months, the exchange banks would obtain a return of 5 crores a year.

industries and commerce of the country may have their necessary " sinews of war " is becoming more prominent than before. As this national sentiment becomes growing in intensity, the Imperial Bank itself might be asked to finance our foreign trade and the present restrictions hindering the undertaking of general exchange business might be removed.

Our commercial banks would not be undertaking a business dangerous to their existence, if they were to compete with the exchange banks for this exchange business. Although the conversion of foreign trade money into domestic and *vice versa* is somewhat difficult as the element of speculation always enters in exchange transactions between countries having different metallic currencies, although various influences operate on the rate of exchange, yet it can be safely conducted if the banks realise the complicated nature of the business they have to perform and perform it with due caution.

Suggestions to overcome these difficulties.

There should be an equal division of labour in the matter of discounting and handling internal and foreign bills of exchange. While the discounting of internal bills of exchange is not accompanied by any serious risk, provided these banks discount first class trade bills arising out of genuine trade transactions, the theory of banking dwells on the difficulties attending on the operations in foreign exchange and advises that "bills" arising out of export and import, *i.e.*, foreign trade and internal trade are to be handled by different institutions, the former by the exchange banks and the latter by domestic banks. It

presupposes an intimate knowledge of the trade relations between the two countries and this can be grasped only after several years' experience. The relative value of the two currencies of the trading countries should be fully known and any likelihood of trading expansion in the near future should be clearly realised.

Dealings in Futures.

Besides overcoming these initial difficulties the banks that undertake this business should avoid speculation in exchange on their own account. They should be careful in keeping their purchases and sales of exchange for various dates of delivery as nearly equal as possible. Occasionally they can make an excess of sales or purchases but broadly speaking an overbought or an oversold situation is not advisable.

For a safe and efficient performance of this, business branches in foreign monetary centres are necessary and the incidence of cost of such branches is very high in the beginning. Agents can however be employed but they might mismanage.* The foreign exchange department must be in the hands of a trained specialist. Clerks possessing good knowledge of foreign languages are necessary. The domestic needs or policy of the bank should be borne

* The Alliance Bank of Simla which failed recently was forced to open a bank in London on account of Messrs. Boulton Brothers and Co., who have locked up their money in their operations in the London Money Market. As the Liquidators' report is not yet published (1st March, 1924) nothing definitely can be said against the management of the said private firm which had to be taken up by the Alliance Bank of Simla.

in mind by the head of the exchange department of the bank and it is difficult to keep both the domestic and foreign operations of the bank each involving large outlay of capital, in close harmony with each other.

Provided our commercial banks do not underrate these difficulties, there would be nothing unwise or inherently unsound in their proposal to undertake exchange business.

TABLE SHOWING THE PROGRESS OF THE EXCHANGE BANKS.
£ (1,000).

Year	No of Banks	Paid up Capital	Reserve	Deposits	Cash balances	
				In India	Out of India	In India
1915	11	22,681	14,112	335,456	45,111	76,013
1916	10	22,836	15,095	380,388	41,367	101,401
1917	9	18,384	14,298	533,753	54,765	337,437
1918	10	22,269	17,180	618,560	57,981	151,755
1919	11	31,931	21,139	743,590	63,571	290,832
1920	15	54,198	36,099	748,071	84,197	251,753
1921	17	66,369	45,263	751,961	82,318	235,674
1922	18	66,541	45,680	733,844	91,654	161,763

This table is taken from the Statistical Tables relating to banks in India, 1922 issue.

CHAPTER IV.

THE INDIAN JOINT STOCK BANKS.

Indian Joint Stock Banking is barely a century old. The principles of Joint Stock Banking were first introduced into this country by the Agency Houses, some of which did banking business along with trading business in the early beginning of the nineteenth century say 1810—1835. Mr. Thomas Bracken, a partner in the house of Alexander & Co. while giving evidence before the Select Committee of the House of Commons* relates the history of the Agency Houses thus: " The Agency Houses were chiefly formed of gentlemen who had been in the civil and military services who finding their habits better adapted for commercial pursuits, obtained permission to resign their situations and engage in agency and mercantile business. They received the accumulation of their friends in the company's service. They lent them to others or employed them themselves for purposes of commerce, they were in fact the distributors of capital rather than the possessors of it. They made their profits in the usual course of trade and by difference of interest in lending and borrowing money and by commission. In course of time carrying on successful commerce many became possessors of large capital and returned to England having most part of it there. The Agency Houses became the usual depository of a great portion of the savings

* Select Committee of the House of Commons, 1833, Volume III.

and accumulations of the civil and military services in India."

Not all the Agency Houses carried on the banking business but only a few and the Bank of Hindustan which was formed by Alexander & Co. in 1770 had the right to issue bank notes.* But a great many of them performed the three functions of—(1) receiving deposits, (2) paying drafts, (3) discounting bills. The real impetus to the starting of banks was given in the year 1813 when an act was passed removing the restriction on Europeans settling in India. Several banks were started but during the troublous period of 1829-33 many of the Agency Houses failed. There was "gross mismanagement, wild speculation, and extravagant living"† on the part of these big merchant princes who conducted banking business. Loans were granted to sugar and indigo plantations, to mercantile firms and to people in and out of the service of the East India Company. Reckless speculation was carried on with their money in agricultural, building business and dock constructions. When the mercantile firms and Indigo houses failed in 1829 they also pulled down the Agency Houses with them.‡

* C. N. Cooke says, "its notes though not recognised by the Government had a local circulation amounting to Rs. 50,00,000 for many years they were received at all the public offices in Calcutta scarcely excepting the treasury itself. This bank failed in 1832." *Vide* Banking in India.

† *Vide* J. W. MacLellan's article on Banking in India—Bankers' Magazine, 1893, pp. 50-58.

‡ Alexander and Co. failed for 34 lakhs, Colvin and Co. for 12¼ lakhs, Mackintosh and Co. failed for 25 lakhs, Palmer and Co. for 26 lakhs and Cruttenden and Co. for 13½ lakhs.

The Union Bank which arose out of the ruins of the Agency Houses fared no better and it had to close its doors in 1848. The First Bank of Benares also failed ignominiously owing to fraudulent and criminal mismanagement on the part of its officers.*

Undaunted by these failures new banks were started and these did much useful business. The Agra Bank (1833-90), The Simla Bank, 1844, The London and Eastern Bank 1854, The Commercial Bank 1854, The N. W. Bank 1844, The Dacca Bank 1846-62, were some of the important banks doing business at this time. But these could not develop their business satisfactorily to meet the currency needs of commerce owing to the hostile attitude of the court of directors of the East India Company which never wanted these banking institutions to act as rivals in the matter of their exchange business. Though the court ceased to be a body of merchant princes, yet this traditional attitude of hostility stood in the way of their growth. Although these banks had the privilege of issuing notes, their issues were small.†

* A detailed account of the causes leading to their failures is given by G. F. Shiirras in his Indian Finance and Banking, pp. 352-354.

† Mr. R. M. Martin in his "Indian Empire" gives the following table relating to the issue of notes by the then banks—Volume I, p. 565.

Name of the Bank.	Year of est.	Head Office.	Branches.	Paid-up Capital.	Notes.	Bills.
				£	£	£
Bank of Bengal.	1809	Calcutta	...	10,70,000	17,14,771	1,25,251
Bank of Bombay.	1840	Bombay	...	5,22,000	5,71,089	1,95,836

The Great Sepoy Mutiny of 1857 unsettled the country for quite a long time and no banks could arise. But in Bombay, thanks to Lancashire money that poured in for our cotton many banks arose in the years 1864-66. These could not withstand the speculative tendencies of the time and fared miserably.* The First Bank of Bombay also had to close its doors in 1866.

At about this time, some of the exchange banks were started in London to conduct banking business in India and with the exception of these no big Indian Joint Stock Banks were floated. Hardly was quiet restored in this country when the exchange trouble began to occasion serious loss and the minds

Name of the Bank.	Year of est.	Head Office.	Branches.	Paid-up Capital.	Notes.	Bills.
				£	£	£
Bank of Madras.	1843	Madras	...	3,00,000	1,23,719	59,871
Agra and U. P. Bank.	1833	Calcutta	Agra, Madras, Lahore, Canton, and London.	7,00,000	...	...
N. W. Bank	1844	Do.	Bombay, Simla, Mussorie, Agra, Delhi and Cawnpore.	2,20,000	...	...
Delhi Bank	1844	Delhi	London, Calcutta Bombay and Madras.	1,80,000	...	...
Simla Bank	1844	...	...	63,850	...	...
London and Eastern Bank.	1854	...	...	2,50,000	3,25,000	...
Comercial Bank.	1854	Bombay	London, Calcutta, Canton and Shanghai.	4,56,000	...	...
Mercantile Bank.	...	Do.	London, Calcutta, Kandy, Canton and Shanghai.	3,28,826	7,77,156	1,09,547

* Sir D. E. Wacha, "Bombay Municipal Government," pp. 21-22.

of all people even that of the Government had to be turned to the pressing problem. Thus 19th century history did not afford any scope for the serious development of banking business in India.

The history of the Indian Joint Stock Banks for which Indians have been responsible begins from the year 1881 when the Oudh Commercial Bank was founded. Some other banks were established at about this time. The Punjab National Bank was established in 1894. The Peoples' Bank was founded in 1901. The Amritsar Bank was started in 1904. It was in the first decade of this century that a serious impetus was given by the "Swadeshi" movement to the starting of indigenous Joint Stock Banks. The prosperity of Northern India, increased on account of the opening of the canal colonies and the development of export trade in wheat had rendered possible the investment of capital in banking companies.

Large and small banks were established all over the country.* The banks were merely considered as instruments by which the people could become rich all of a sudden. But their disillusionment came during the crisis of 1913-1915 when almost every one of these mushroom banks was severely put to a test.

Name of the Bank.	Head office.	Date of Regn.	Paid up Capital (lakhs Rs.)	Deposits lakhs.	Branches
The Bank of India ...	Bombay	1906	50	470	...
*The Indian Specie Bank ...	Bombay	1906	75	270	...
The Indian Bank ...	Madras	1907	101	41	4
The Bengal National Bank ...	Calcutta	1907	3	30	4

* These have gone into liquidation.

Name of the Bank.	Head office.	Date of Regn.	Paid up Capital (lakhs Rs.)	Deposits lakhs.	Branches
The Punjab & Sind Bank ...	Amritsar	1908	3	30	4
The Bharat National Bank ...	Delhi	1908	4	1	6
The Bank of Northern India ...	Rawalpindi	1908	1	6	5
The Bank of Baroda ...	Baroda	1908	10	†	†
The Bombay Merchants' Bank	Bombay	1909	15	1	2
*The Credit Bank of India ...	Bombay	1909	19	51	†
*The Ahmedabad Banking Corporation	Ahmedabad	1910	7	23	†
The Central Bank of India ...	Bombay	1911	25	357	6
*The Standard Bank ...	Bombay	1912	10	†	†
The National Financing and Commission Corporation	Bombay	1912	11	36	1
The Bank of Mysore ...	Bangalore	1913	10	61	7

This table is taken from the Banking Blue Book. All these banks are due largely to the swadeshi stimulus arising out of the partition of Bengal.

The Locale of these Banks.

These Indian Joint Stock Banks are to be found mostly distributed in the Punjab, United Provinces and Madras and in the three presidency towns of Calcutta, Bombay, and Madras. Rangoon, Karachi, Lahore, and Cawnpore have a great number of banks and a clearing house exists in the seven above-mentioned places. There are very few Joint Stock Banks in the native states. But the Banks of Mysore and Baroda are doing creditable service in providing banking facilities for the people of these native states. Modern Banking facilities exist only in 165 places and in most of these big cities there is much of overlapping.

* These have gone into liquidation.

† Figures not available.

The Business of these Banks

Generally speaking these banks have two functions before them—(*a*) to develop the money power of the people and (*b*) to provide credit for the millions of people of our country. Thus their main business is to attract deposits and finance internal trade. In the Punjab an attempt was made to finance industries but it proved a failure. They attract deposits for which they pay 4 to 5 per cent. for fixed periods above six months and two per cent. on current accounts after stipulating for a minimum monthly balance, say, 200 or 300 rupees. Though there is no authoritative statement explaining the nature of their business* it can be presumed that they minister to the needs of their clientele and much depends on environment and the intentions of the founders and the managers of these banks.

Bank Failures.

Most of these "Swadesi" Banks were viewed with jealousy and disfavour and the old banks refused to lend a helping hand in times of trouble. As Lala Mulkraj says, "The political history of India got repeated in the attitude of these banks towards each

* A close perusal of the balance sheet of these several banks will reveal to us that they have been conducting the following lines of business: (1) keeping current accounts, (2) receiving deposits, (3) discounting inland bills of exchange, (4) advancing money on securities and Government paper, (5) acting as agents, (6) issuing letters of credit, (7) undertaking the purchase and sale of Government, Stocks and Shares on behalf of their customers, (8) realising dividends for their constituents, (9) holding things for safe custody, (10) remitting money, (11) encouraging small savings.

other." The official committee of Lahore appointed to enquire into the causes of the bank failures in the Punjab writes that "during the crisis there was no co-operation between the Indian banks themselves or between them and the English banks or between them and the old-fashioned Indian banks." Mr. Lala Harikishan Lal says* that "the old banks brought the new ones to trouble and did their best to eliminate the new comers." Lala Mulkraj says "there were formidable forces arrayed against Indian Banking in 1912. A destructive genius in the person of Rai Bahadur Moolraj arose to destroy all banks, good, bad, or indifferent. He exploited all the forces that could be commanded for destruction. Tongue and pen were both used freely and a religious paper was got under control and converted into a weapon for the financial ruin of the country. This fright created mistrust and a run upon Indian banks commenced." The Presidency bank of Bengal refused to lend even on Government security in spite of the favourable recommendation of its Lahore branch.

Whatever might be the reason, there was a widespread failure of these banks† during the years 1913 to 1915. Of all the banking crises which India has experienced, that of 1913 to 1915 was the

* *Vide* Lala Harikishan Lal's presidential address at the Indian Industrial Conference.

† The first big bank that closed its doors was the People's Bank in the Punjab with no fewer than 80 branches and a crore of deposits. The Credit Bank and the Indian Specie Bank were some of the other big banks which failed during this crisis. The Amritsar Bank was closed in 1913. In India about 63 banks failed during this crisis.

most disastrous one. In 1829 to 1832, in 1857 and in 1863 to 1866 there were banking failures. It is true that much capital was lost during these times. In the 1913 to 1917 crisis "no less than 34 per cent. of the total paid-up capital of the Indian Joint Stock banks has been lost."* Many of the depositors were ruined. The Indian people have again to be educated towards banking business and the banking habit has to be created afresh. This widespread failure gave scope for the statement "that Indians are incapable of managing Joint Stock Banks." Pandit Madan Mohan Malavya gave a crushing reply to this charge.† Such failures have occurred in all countries and they are indispensible concomitants to the early era of Joint Stock Banking.‡ Indian Banks have failed even though they had had European Managers. According to Lala Harikishan Lal three or four dozen banks managed by Europeans have failed in this country during the last hundred years."

A close study of the causes for their failures will reveal the fact that mismanagement due to inexperience in banking affairs accounts for the most cases. The official committee of Lahore says, "all the evidence produced before us insisted on the want of business knowledge and inexperience in company

* *Vide* G. F. Shirras—Indian Finance and Banking.

† *Vide* Minority report of the Indian Industrial Commission.

‡ During the early days of banking in England many of the country banks failed. There were 425 bankruptcies in 1726, 446 in 1727 and 338 in 1728. Several country banks failed in 1814 to 1816 period. In America during the years 1865 to 1911 about 51 National banks of the United States of America failed.

promoters, managers and staff as a primary cause of failure. There were few competent managers, whether of banks or of industrial concerns. Consequently egregious blunders were made and some of the so-called dishonesty seems to us very like ignorance, much of it was due to anxiety to cloak losses.'' The inexperienced Directors did not discharge their duty. The incapable managers were unable to do their work properly. The ignorant shareholders could not satisfactorily exercise their rights and duties.

Most of the Directors that were elected to supervise the manager's work and help him with their advice were wrongly chosen and they were easily led away by the opinion of the manager. There was a story current in the Bombay trading circles that the Director of one bank did not know English, and when the proceedings of the board were being conducted in English, he simply voted blindly on the important questions he had to decide. Such kind of men could never influentially dictate the banking policy. Of course we had no "guinea-pig" Directors but still the first batch of Directors of the Indian Joint stock banks knew little of this banking business* conducted on the Joint stock principle. These

* The first acknowledged duty of the bank Directors is to see that the funds of the bank are safely employed. They should be men possessing reliable knowledge of accounts, business and general working policy of the bank. They should not interfere too much with the administrative routine of the office. They must realise that the Secretary's opinion is entitled to great weight but at the same time they should not be carried away by his wishes. They should have moral courage to refuse better terms to a Director than an ordinary borrower.

Directors were no doubt successful merchants or were men distinguished in one walk of life or other but the mere fact that they have managed one kind of business successfully is no guarantee of their ability to work as Directors of a Joint stock bank.

The managers of the banks were incapable men and had very little knowledge of banking theory. No doubt they were men of some experience but an efficient manager of a joint stock bank should possess these sterling qualifications to make his bank a successful one.* It has been stated that these managers were dishonest and selfish but Mr. Balak Ram Pandya† Auditor of Accounts, Lahore, refutes the charge emphatically. Lala Mulkraj, the manager of Doaba Bank, testifies to the integrity of

* According to George Rae "the bank managers should possess these following qualifications. There should be total absence of bias religious, political or social in his mind. He should be quick enough to perceive any change in the circumstances of the customers. There should be no hesitating dubious and capricious manner. He should be never indolent. Whenever he is in doubt as to the safety of a transaction he should give the bank the benefit of doubt. He should never fly into a passion or bandy words with customers. He should see that all customers are treated respectfully by his officers. In short he should not tolerate any insolence of office at his bank." Many of our managers did not possess these essential qualifications.

† In his evidence before the Indian Industrial Commission he says "when we compare the recent bank and industrial failures in the Punjab with similar incidents in other countries, we are astonished at the comparatively small proportion of cases in which the failures in our case were due to dishonesty or selfishness. The price we have paid for our inexperience is undoubtedly heavy but it is by no means heavier than what other countries paid before us. If we have learnt the lesson which the disasters of the last few years so impressively teach, there is surely no room for despondency."

the staff in the following language * ; as for their integrity I may mention that during the 10 years life of the Punjab Co-operative Bank, out of a staff of 11 officers only one man was guilty of defalcation of a few hundred rupees.''

The Indian shareholders of the Joint Stock Banks never knew their duties properly.† The shareholders should realise that they are co-partners with many others. Their duty is to " put the saddle on the right horse " and see that the officers of the bank are doing responsible duties in right earnest. In no case should they entrust too much power to their manager. They should not place too implicit a confidence in their salaried staff to question their doings. Again many of them were not in a position to scrutinise the balance sheets of their bank and climb over the " balance sheet dodge " as it is styled. They did not choose their men well. The secret of banking success lies in choosing the best men and trusting them completely.

Some other causes have hastened and accelerated the downfall of the banks. The difference between the " paid-up capital, subscribed capital and

* *Vide* His evidence before the I. I. Commission—Punjab Volume, page 290.

† George Rae enumerates the following duties of the shareholders; " he should make no line of hostile remark against the bank in times of run. Whenever he hears a bad rumour, he should in the first instance convey it to the manager. He should not give currency to any calumny against his bank. He should be the guardian and police of banking credit. His duty is to stand by his bank in times of panic. He should not sell the shares at the time of a panic for he would become a bell-wether followed by a score of sheep like himself. His primary duty is to increase the business of his bank and bring more customers to it." *Vide* " Country Banker."

authorised capital" was acting as a handicap from the beginning. As the law did not check this mal-practice, they took advantage to trade on the ignorance of the public who were unaware of the difference between the three kinds of capital. To curb this mal-practice a heavy stamp duty has been recommended by Mr. J. M. Keynes.*

In addition to this every bank should be forced to have a certain amount of minimum paid-up capital, say 50 per cent., before it commences its business.† While the paid-up capital was small the incidence of cost was very high.‡ Liberal salaries, travelling and halting allowances, high commissions to agents and canvassers were paid.

Some of the banks contracted the practice of lending money on their own shares. The failure of the first Benares§ Bank and that of the Credit Bank of Bombay are attributed to this pernicious practice. It is a matter of great satisfaction to see that the Imperial Bank is not allowed to lend money on its

* *Vide* J. M. Keynes, Indian Currency and Finance, page 232. "The stamp duty should be proportioned to the nominal capital. He instances the case of a comic opera bank registered in Calcutta in 1910 with about £20,000,000 without having any paid-up capital at the time of the last return.

† Such a rule prevails in the Canadian Banking system. The minimum required capital is $500,000 of which all must be subscribed and one half paid before the bank commences its business.

‡ "In the case of many of the Punjab banks the capital was seldom higher than 4 or 5 lakhs. The Peoples Bank had 80 branches. The result was that the money cost them at least 12 per cent. 6 per cent. they paid to depositors and their expenses amounted to at least 6 per cent. on the capital." *Vide* The evidence of Lala Damodar Dass—Volume 5, I. I. Commission, page 254.

§ It should not be confused with the present Benares Bank which is doing business on sound lines

own shares, though they may be taken up as an additional security for covering loans. The charter of the Imperial Bank of Japan forbids the making of loans on the security of its own shares or purchasing the same.

In some cases there was no strict auditing of the accounts. It was a mere farce and the auditor to secure the favour of the manager, was lax in his duties and connived at the bad practices of the managers.* The auditor should be a man of much experience in the science of book-keeping and the analysis of accounts. His main duty is to place the facts as they appear to his light. He should be "the detective of the shareholders who should keep a vigilant eye on the Directors always." The auditors should see that the Directors are not nursing huge and growing accounts year after year long after they have become doubtful. This is the grim skeleton in the banking cupboard and he should expose it to the shareholders.

Some of the banks indulged in speculative commitments.† The Indian Specie Bank's purchase of silver and its attempt to corner silver became a miserable failure and led to the closing of its doors.

* *Vide* The evidence of Lala Damodar Dass: "The bank of Peshawar and the Hindustan Bank gave out false balance sheets and this is rendered possible because the auditors who audited the accounts were not real auditors in the true sense of the word. They were merely accountants." *Vide* page 258.

† "The excessive loans made to the cotton ginning factories were properly speaking speculations." The Hindustan Bank of Lahore granted loans to the Punjab Musical Association, Ltd. (a theatre with no capital), and to the Punjab Bros. Co. (a speculative shop in Karachi). *Vide* p. 254, Volume 5, Indian Industrial Commission.

This was one of many factors which brought about its downfall.

Many of the banks were performing quite the opposite of commercial banking business. Instead of making all their assets easily realisable or keeping them in a liquid shape, they locked up their funds so that they were no longer " quick assets." What the commercial bank should aim at is " immediate convertibility." All the short-dated deposits can be demanded at any time and it is unwise to invest them in long-dated loans to industrial companies.* The bank managers failed to realise the vast difference between " immediate " and " ultimate " convertibility. The substitution of the latter for the former means the question of life or death to the bank. They sacrificed the principle of liquidity which should be borne in mind by every banker. Instead of constantly controlling the liquidity of the resources at short intervals by frequent general inventories with the greatest care and instead of keeping a proper composition of security and holdings in their portfolio against their total obligations, they locked up their money. According to Dr. Reisser " the security and maintaining of the liquidity of the assets is a most essential task incumbent on the banker. Indeed in view of the variety

* Both the Punjab National Bank and the Co-operative bank lent about ten lakhs to a single gentleman who started a network of ginning, cotton factories and presses and put up flour mills. 90 lakhs of rupees out of a crore or so in the Peoples' Bank has been sunk in machinery and buildings and the liquidators would not get even half of that money in less than ten years. *Vide* The Evidence of Lala Nanda Lala Puri, also the Evidence of Lala Damodar Das.—Volume 5, Indian Industrial Commission.

of claims made on the resources of bankers and banks and of the multitude of aims pursued by them, it is one of the most difficult problems of banking policy. It is all the more difficult since the establishment of the right proportion of the so-called quick assets to the liabilities specially obligations falling due at any time or within a certain period, does not always depend solely on the will and discernment of the bank. Possibilities have to be reckoned with, for instance, that the issue of new shares required to restore the necessary liquidity of the banks' resources after a great increase of business is impossible during bad or critical times; that consequently its assets would be tied up just at the very moment when it might be called upon to relieve general embarrassment by proper intervention."* Several of the "swadeshi" banks were not in a hopelessly rotten state and this can be proved by two facts. The survival of the Punjab National Bank shows what an Indian Directorate and staff are capable of doing in trying circumstances. Many of the liquidated banks have paid in full.†

Most of these Indian Joint Stock Banks paid a very high rate of interest to the depositors. The Bank of Burma undertook to pay 6 per cent. on deposits. In order to earn this business out of the banking line had to be conducted and this precipitated its downfall. In the Punjab there was a regular competition to get deposits. In order to induce several poor widows and orphans to deposit their

* Dr. Reisser "The Great German Banks"—American National Monetary Commission Report.

† The Marwar Bank and the Punjab Co-operative Bank.

money the banks paid 8 per cent. under various pretexts.* They had to lend at a very high rate of interest and lending on a high rate they could not have good security. Ruinous rivalry produced by competing deposit rates forced the banks to entertain illegitimate business.

In some cases notably two or three, banking business included "medical attendance and coach-building." The Honourable Sir J. Smith of the Allahabad Bank † said that "an institution has no right to be called a bank which undertakes coach-building, ekka repairs and medical attendance, the manufacture of soap and oil and certain things from machinery or engages in trade or manufactures—of any sort even though it be stated as follows ;—"The leasing, hiring and purchasing of all commodities and substances which can form the subject of purchase or sale." The bankers' profession is to take care of the community's capital and to turn it to good account, that is, to make it productive, particularly by placing it at the disposal of others engaged in production.

The Presidency Banks did not realise their function of being "residuary trustees" and bankers' banks. As Mr. J. M. Keynes has said "they are not strong enough to support the whole

* If the deposits belonged to minors, widows, orphans or charitable institutions they would give eight per cent. While the Bank of Bengal rate was on the average about 4 per cent., the Punjab banks did not care to regulate their rate for deposits in conformity with the standard rate. On the Bombay side however the deposit rates were governed by the Bank of Bombay rate.

† *Vide* his evidence before the Indian Industrial Commission—(The United Provinces)—Volume.

burden" and their apathy towards the struggling Indian Joint Stock Banks has been criticised by the Lahore Committee in its evidence before the Indian Industrial Commission.

Some of the Indian Joint Stock Banks were got up to satisfy some transitory caprice and did not arise to satisfy the legitimate banking and trading requirements of the people. In the city of Bombay some banks arose in this way because the powerful magnates who were not included in the directorate of a bank, got up another one under their patronage and were thus the creation of interested parties.

The jealousy of the Exchange Banks, it has been said, is responsible for the failure of the Indian Specie Bank. This Bank under the able guidance of the late Mr. Chunilal Saraiya opened a branch in London with a view to facilitate its business in pearls and silver. The Exchange Banks resented competition in the exchange business and the rate-cutting that ensued is held responsible for its failure. But as a matter of fact, its speculative purchases of silver and the refusal of the Government of India to buy silver at its hands have precipitated its downfall. This bank lost heavily in loans advanced to jewellers and the *badla* business of Fazul and David shares.

In some of the Indian Joint Stock Banks, the bank officials took too much of the loanable money and invested it in their own enterprises.* The

* "Of the total advances of Rs. 10,709,000-14-1 we find that no less a sum than Rs. 7,172,687-13-1 have been advanced to Companies or other concerns in which certain directors of the Bank have been interested either as individuals, directors or as joint borrowers"—Liquidators' report relating to the Peoples' Bank.

failure of the Lahore Bank, the Doaba Bank, the Hindustan Bank (Lahore) and the Industrial Bank was due to this fault. The Bank of Burma failed in 1911 and out of a total working capital of 1 crore 19 lakhs it advanced ⅓ of it to a firm in which the directors were interested. The sinking of too great a proportion of the bank's funds in one industry is a grave evil and this had not been heeded by the European manager of the above bank. No bank should commit the fatal mistake of "placing all its eggs in one basket." It should never get itself entangled in one or two or three huge and over-mastering accounts, the smashing up of such a big customer would spell disaster to the bank. During the course of everyday run of its bills, advances, overdrafts and investments some bad debts may be created here and there but these will not be a matter of serious concern. A bank should be careful in "distributing" its risks as Dr. Reisser puts it.

Excessive interconnection and the interdependence of banking and industrial concerns under a board of common directors as in the case of the Punjab companies is fraught with harmful results. It is unsound in principle that lenders and borrowers were to be the same persons.

Some of the Joint Stock Banks had not only enormous nominal capitals but they combined high-sounding titles with it so as to mislead people as to the actual strength of their institutions. A recent instance of a bank making a "colourable imitation of the name of another bank came up for judicial enquiry. Mr. Justice Mulla refused to permit the

defendant bank, *viz.*, National Bank of Indore for carrying on business under that name.

Many of the Indian Joint Stock Banks had not adequate resources against deposits and the percentage of cash to its liabilities was only 11 per cent. and in some cases it was lower than this. The Exchange Banks and the Presidency Banks kept a much higher percentage of cash against liabilities than this 11 per cent. The Indian Joint Stock Banks have not understood the problem of banking business. As one eminent banker says " if the banks were to keep in cash all the money deposited with them business would come to a standstill and a crisis would ensue. If on the other hand banks were to lend all the money on deposit with them a general panic and collapse would follow after a short period of overstimulation. Between these extremes lies the middle course, the finding of which is the problem of banking."

In some cases " dividends were paid out of the deposits that were coming to the bank for the capital of the bank had disappeared long before this time. The balance sheets of some of these Indian Joint Stock Banks were very good instances of window-dressing. Some banks manufactured blooming balance sheets showing a large amount of assets whereas these banks were really working at a heavy loss. The practice of paying dividends when they were not earned was not given up."*

Such and similar instances of mismanagement and lack of proper organisation of the banking business can be quoted but the " two primary causes

* *Vide* the evidence of Rai Bahadur Lala Damodar Das, Indian Industrial Commission—Volume 5, p. 225.

that led to the collapse of the banks are (1) the inexperience and the defects of the machinery inevitable to the starting of a new venture, (2) the lack of palliative or remedial action such as Government itself or quasi-Government agencies, *i.e.*, a state-supported provincial bank might supply."*

Again the practice of mutual drawing of accommodation bills between the various banks which we meet with in the foreign money markets would have been of some help to the sound banks.

The failures of these Indian Joint Stock Banks led many people to agitate for banking legislation binding on the banks for the proper conduct of their business and that an expert banking committee should be appointed. One extreme school of thought inclines to the view that the Government should train people in banking matters by establishing model banks, regulating other banks and that strong banking laws should be passed to prevent dishonesty and fraud.

The Rationale of Banking Legislation.

Banking is of high antiquity but our ancestors were familiar with banking credit; at least history credits them with that knowledge. Archeologists have discovered clay tablets of credit that were in use in Assyria.† Students of Manu, the famous Indian Lawgiver, are familiar with his well-known laws regulating the use of credit. The Athenian money

* *Vide* The evidence of the Official Committee of Lahore before the I. I. Commission.

† Collin's Banking Law—Collin says that one Egibi and Co. acted as the National Bank for the Babilonian Monarchs. These baked clay tablets are preserved in the British Museum.

changers did business somewhat closely akin to modern banking business. Xenophon implanted the idea of a bank but he was too far ahead of his time. In the Argentarii of Rome can be seen the nearest possible approximation of a modern banker. The barbarian invasions of Rome and the ensuing unsettled conditions of Europe during the Dark Ages must have prevented the early development of banking business. During the Middle ages, the money changers of Italy revived their business and the Jews, thanks to the persecutions of all the continental countries perfected the beautiful bill of exchange. The successful lead of the Italian Merchants and their religious zeal to collect papal dues while acting as the emissaries of the Pope in the continental countries led to a very extensive use of the bill of exchange. To Italy belongs the credit of having founded the First Banks, *viz.*, The Bank of Venice (1167) and the Bank of Genoa (1345). The Italian money changer, the Jewish money lender and the Lombard Street Financier are the important connecting links in the banking chain. With the advance of centralisation in commerce and in national life the necessity for public banks arose. The development of manufactures and rapid growth of international trade led to large, scale banking, and to-day banking business is regarded as an honoured profession and it has received such a wide and varied form that it is hard to believe that our ancestors were familiar even with the rudiments of banking credit.*

* When the learned writer MacLeod said that "banking in the modern sense of the term did not exist before 1840" he probably meant this thing.

If banking business is of such hoary antiquity and if state regulation of bankers and banking credit was well known to our ancients as evidenced by the Athenian regulations, the Code of Manu and the Justinian laws * the modern state ought to feel ashamed at the perfunctory manner in which it attempts to control the modern banking business in the interests and well-being of the nation.

Besides this historical justification, there is another cardinal reason why the state should control banking business. The modern banks can make or mar the future of a nation. With the entire credit mechanism of the country controlled by it, with the whole floating capital of the nation deposited in its hands, with " the nation's material future " entrusted to it and the " fate of the nation lying on its lap " the modern banking system is indeed a vitalising force which if exerted in the right and proper channels is fraught with immense possibilities. With a judicious selection of their customers and with timely loans to them they can build up the manufactures of a country and direct capital and labour to the most productive channels. By creating thriving industries they can add to the national wealth of the people and bring contentment to the wage-earning labourers. They can accomplish all this and more.

* According to the Roman law each family had to maintain a ledger in which the head of the family had to keep a record of borrowed money, or money lent, all profits or losses or any disbursements of any kind. These ledgers were the only legal evidence in a court of justice and it is from this custom of book keeping that the modern credit system has developed.

But their power to do harm in case of misdirecting capital encouraging speculation and wrongly investing is no less considerable. What the State aims at by wisely directed banking legislation is to maximise the advantages of sound banking and help the banks to better perform their task. Modern banking is a quasi-public service to be watched and properly regulated. The anxiety of the State is to see that banking accommodation is extending to all the deserving persons on equal terms. Banks are public utilities, intended to distribute their resources mainly with an eye for the public benefit.

The failure of a bank creates a vicious circle and ruins several people. Though the State recognises the impossibility of legislating to prevent failures yet it attempts to prohibit banks to do business of an unsafe character or alien to legitimate banking business.

The State while passing laws of a restrictive nature forbidding the banks to do as they like, is not altogether unmindful of the interests of the bank. It recognises the social services of the banks and gives them special facilities. The special laws about the negotiable instruments and other concessions shown to them, as the general lien of the banks, the law of Estoppel and the Bankers' Book Evidence Act are an evidence of this grateful recognition. While treating them very leniently the State does not forget to restrain effectively their power to do harm to the public by their own indiscretion. General laws are passed so as to attain uniformity and prevent favouritism.

Banking legislation extends from the Central Bank right up to the ordinary Joint Stock Banks.

The Central Bank is always made to work under special provisions incorporated in a separate charter. The ordinary Joint Stock Banks are incorporated under another law common to all of them. Private banks escape vexatious Government control in almost all countries. Their importance is however dwindling day by day. So long as they are under able financial guidance they earn the gratitude of their country. But the continuity of such able financial guidance is not assured in all cases and many ignominious failures have occurred in the past. Hence private banking is diminishing in importance. In England* and America public opinion is decidedly against them and they are virtually forced to amalgamate themselves with other concerns by virile competition prevailing in the money market. Here, as elsewhere the case of India forms a notable exception. In India the private bankers (indigenous bankers as they are styled) are going on as usual and they are still a powerful element in our banking system to-day.

The case of the Joint Stock Banks is different. They are under able financial guidance and influential directors can mould these institutions into such a shape as to bring about the greatest good of the greatest number of people in a given society. The necessity to earn profits must force the banks

* Bagehot says "there has probably very rarely been so happy a position as that of the London Private Banker and never perhaps a happier." This remark might have been true in his own time but to-day the demand for greater publicity and greater security for associated capital is working against the private banks.

towards progress tempered with caution.* Hence Joint Stock Banks are on the increase everywhere and they are increasing in our country as well.

The main reasons why the State is so solicitous to procure sound banking conditions have been set forth already. But something more must needs be stated to explain why Joint Stock Companies conducting banking business are differentiated from trading companies and treated separately. One law does not suit both of them because the banks are lending institutions; they create and protect credit. While Joint Stock Trading Companies borrow money and try to exploit credit. So banking companies have special safeguarding rules to protect and help them.

While usually one law is considered sufficient as regards the process of formation of trading as well as banking companies, the latter are subject to additional legislation of a very detailed character. Very careful prescriptions of law extending to every important item of banking business are laid down in order to bring about full trustworthiness of these banking companies. The amount of capital, the accumulation of reserves, the character of loans and

* Lord Overstone writing in 1832 says, "Joint Stock Banks are deficient in everything requisite for the conduct of the banking business except extended responsibilities." Bagehot commenting on this statement says that "the bankers of Lord Overstone's time lent much to private individuals from whom no security could be obtained. The banker acted on his judgment of discretion, the sense and solvency of those to whom he lent." But now the banks have ample material to judge the standing of the borrower. Credit information of a high order can be obtained easily. It is possible to scrutinise the Balance Sheet and bearer securities can be taken as collateral for covering loans.

discount business, the nature of the cash reserve and its proportion as against the liabilities of the bank and the very quality of the investments of these banking companies are all subject to stringent regulations for the following reasons.

The Capital of a bank is the money subscribed by the shareholders. It stands virtually as a guarantee to the customers of the bank inspiring them with confidence. Banking business is purely a question of mutual confidence between the depositors of the bank and the banker himself. It is very often known as the " big confidence game." Banking business consists in lending others' money and as Lord Overstone says " banking business is a business of the brain with other peoples' money." A paucity of capital will not enable the banking institutions to execute its tremendous task of responsibility and trust efficiently, hence the legal regulations against inadequate banking capitalisation. In the case of new banks, there is always an impairment of capital for the first few years as expenses run in excess of interest collections and unless there is a large amount of capital actually paid up at the start, it is difficult to meet with success.

Legislators wish to regulate not only the amount of capital required for the starting of a Joint Stock Banking Company but they also insist that a due proportion, say, one half or one-third of the subscribed should be paid immediately at the start and the balance to be paid within six months at the utmost. Their aim is to prevent the banking company from being handicapped to any extent by

virtue of its meagre capital. A large capital also renders unnecessary "touting" for business to get profits or canvassing for deposits by paying a high deposit rate.

Coming to the Reserve the State aims to compel the banks accumulating a decent reserve in order to help the bank in its own operations. The reserve is virtually the shareholders' property and can be locked up with impunity, and the greater the reserve the greater is the confidence inspired in the minds of its customers as regards the ability of the banks to discharge their liabilities.

A large reserve acts as a buffer receiving all sudden and unexpected shocks such as a great depreciation of assets for which no provision had been made and bad losses greater than the amount of profit earned during the course of the year. The presence of a large reserve on such occasions saves the original capital from being washed away by these unforeseen happenings.

It is by loaning that a bank confers its greatest blessing on society and its business. The strength and safety of the bank depends on the character of the loans it grants. The bank has not only to select judiciously its customers but it must also omit the fatal error of lending too much of its loanable money to any individual firm or undertaking. The object of the legislature—is to see that the bank distributes its risks over several concerns or individuals of the most unimpeachable honesty, financial rectitude and business capability.

Another object why loans by banks to its officers and directors are restricted is to see that no greater

line of credit is granted to them than they can obtain from any conservative banker. Even in the matter of discounting business the anxiety of the legislator is to curtail the freedom of the bank from accepting anything except first class paper or tying up their money in transactions of a spurious character.

Legislators wish to prohibit the banks from lending on the mortgage of real property as it would lead to a locking up of the short term deposit money in long term loaning. Hankey, a practical banker says "the commercial banker has to realise the enormous difference between a bill of exchange and a mortgage of real property." The difficulty of ascertaining the true ownership of these kinds of real property as houses and lands and the legal restrictions that are attendant on the transfer of such property, preclude them from the banker's choice. He has neither the time nor the ability to assess their value carefully and loan on them.

Legislators realise that a wise management of the loaning business conduces to the stability of the bank and enables it to pull on with a small cash reserve and does not lead to an unwise expansion of credit.

The cash reserve of the bank is not only the foundation of any credit that can be created by it but is an insurance fund against risks. It enables the bank to meet any unusual and extraordinary demands made on it by the depositors. The object of regulating the cash reserve fixing its dimensions and even prescribing its actual composition is to enable the bank to better perform its task and as the bank is always saddled with large numerous 'demand'

deposits to be paid, there should be a guarantee that it can meet the depositors' call. The desire to earn profits is very natural and the tendency to reduce the cash reserve almost to the breaking point or "apprehension limit" as Bagehot puts it has to be curbed by laws.

It is true that a legal limit to the cash reserve tends to make it inelastic and any law prohibiting its free use in cases of rare emergencies is meaningless. As Mr. Robertson says "an iron ration which you must not touch even in the throes of starvation is something of a mockery." It generates a sense of false security. By keeping the prescribed limit of cash reserve the bank may think that it has done everything it has to do. But laws should be so framed as to permit a free use of the cash reserve under certain conditions. Cast iron laws do not bring about a better management of the cash reserve but the fact that it is kept and that it enables the bankers to meet some portion of their liabilities is a source of confidence. It limits the field of disaster that may be brought about by injudicious or adventuresome banking. Instead of overwhelming and complete bankruptcy there is something which enables the bankers to dole out to its creditors.

Successful banking is virtually dependent on a careful management of the cash reserve. While recognising that "the cash reserve is dead money and makes no contribution to the dividend" whatsoever, as Professor Foxwell puts it, the bank managers should possess a cool head, sound judgment and a resourceful mind. By constantly adjusting

their discount rate they should bring about satisfactory conditions always. Very few banks realise that it is better to err on the side of caution and provide a large cash reserve, thereby making a part of it idle, rather than be adventurous with a smaller cash reserve. The banks should not rely on their ability and management " to muddle through somehow "—as Lord Rosebery puts it. To avoid failure is far more important than to heap up high and precarious profits. As Bagehot says " adventure is the life of commerce but caution if not timidity is the essence of banking."

As regards investments that is the banks' holding of gilt-edged securities, the object of the legislators is to see that the banks invest their funds in such a way as not only yield profits but see that they are at the same time liquid. Only first class securities are to be held and these should possess absolute strength and safety and be easily marketable with the minimum trouble and risk of loss.

In addition to these laws hampering the freedom of the banks almost in every kind of their business, the State insists on the banks publishing their transactions periodically. Although some of the banks may resort to the pernicious practice of window-dressing at the time of publishing their balance sheets much can be gained by publicity. The furnishing of a well-informing balance sheet which artfully unfolds the tale of progress and increase of business, is by itself the most successful method of attracting customers to the bank. The banks have realised the manifold advantages of publicity and they are coming forward of their own

accord to furnish all details of their banking transactions.

This is the *raison d'etre* of all banking legislation. The State knows full well that the banks cannot be made safe or well-managed automatically by its laws. It realises that no system of examinations can be a perfect one. It always grants considerable latitude in the matter of loans and knows clearly that to impose a dull uniformity without paying any due heed to the changing conditions of different localities will be of no avail. Hence it is wise enough not to descend to details. It is fully conscious of the fact that honesty, integrity and capacity cannot be obtained through the process of legislation. It does not aim to legislate so as to secure people from their own lack of business qualities. Such is the psychology of the bank controlling mind.

It is indeed difficult to explain the absence of any banking legislation in our country. It cannot be attributed to any lack of knowledge in this particular sphere. Our embryo central bank and semi-state banking institution which has recently been created—The Imperial bank is controlled by the State. Its position does not cause any great anxiety, for the State in the fullness of its banking wisdom has retained the old rules of the Presidency Banks' Charter Act of 1876. It is only the position of the newly started and small Joint Stock Banks that is eminently unsatisfactory. Another instance which goes to prove that our State has realised a high conception of its duties towards these banking concerns, occurred quite recently during the days of the

banking crisis of 1913-15. It volunteered help to all the sound banks but the old Presidency Banks through whose medium and intervention the State wanted to help, did not rise equal to the situation. They have cast to the winds the expansive theory of banking which Central Banks ought to pursue during the period of a crisis.

Again their policy of welcoming all foreign banks and extending an open door to them has resulted in much good to our country. These have not only popularised banking business in our country but are the standing monument of a conservative policy standing for slow, sure and steady progress in banking business.

But the non-possumus attitude of our State towards the smaller and newly arisen Joint Stock Banks is hardly creditable to it. The existence of some kind of laws, good or mediocre, would have prevented several failures or at least would have mitigated the intensity and severity of our banking crisis.

Foreign Banking Legislation.

The cardinal reasons actuating the minds of the legislators while framing restrictive laws on the operations of the banking companies have been set forth in detail. It is not the central banks alone that are regulated but banks of deposit also are subject to State regulation. Note issue is generally concentrated in the hands of the central bank and it is everywhere the subject of detailed regulations. The banks of deposit manufacture cheque-currency

which constitutes the important medium of payment in advanced countries and 95 per cent. of the business transactions of modern societies are conducted through the principal means of "the cheque" and it is this reason that must have forced the legislators to turn their attention towards the banks of deposit. This service must be rendered economically, efficiently and honestly by the deposit banks and hence their regulation.

While all countries have deemed it wise to control their note issuing banks if any and their national banks, they differ in their treatment of the deposit banks. The cases of England, of America and India are quite unique.

America furnishes a splendid example of a decentralised banking system buttressed as it were by provokingly detailed laws. In a decentralised system of banking where many individual banks exist with no recognised head, banking legislation is of a minute character and much pains are taken by the State to avoid failures. In addition to State regulations, the banks mutually agree on a common course of action and control themselves by the decisions arrived at in discussions of the Clearing Houses or as in the case of Canada by the Bankers' Association. Thus the State direction is aided by mutual control and efforts are always made to help sound banks in times of emergency.

But coming to the details of banking legislation one finds that the State laws in the United States of America are so varied and different that no adequate idea can be gained of them in such a concise chapter

as this.* The National Banking laws are more uniform, rational and convincing.† Firstly the capital of a bank is graded and regulated according to the inhabitants of the place. For 50,000 inhabitants the minimum capital of the banking company is fixed at dollars 200,000. Next the National Bank Act requires 1/10 of the net profits to be set aside each year till a reserve fund is accumulated to 1/5 of the capital of the bank. As security for the depositors the National Bank Act insists on the double liability of the shareholders. As for note issue any national bank may invest the whole of its capital in Federal bonds and notes up to the par value are entrusted to the bank by the Comptroller of Currency, and any National Bank issuing these notes must maintain a 5 per cent. redemption fund of the face value of the circulating notes, in the hands of the Comptroller. The Act prohibits the banks to lend on real estate. No loan can be granted to a single individual above 30 per cent. of the capital of the bank. An excess of the amount is permitted in case the bank lends on bona-fide bills of exchange and commercial paper owned by the customer. The National Bank Act requires

* The State Banks and Trust Companies are given a wider scope of activity and are subject to close supervision of the State Superintendent of Banks. National Banks are now subject to federal legislation and controlled by the Controller of Currency.

† A good idea of legislation affecting the State Banks and National Banks can be obtained from the Proceedings of the American Academy of Political and Social Science. Vol. I. (1911—pp. 286-290).

15-25 per cent. of all deposit liabilities as Reserves.* In case of the Reserve falling below this minimum discount business has to be stopped. Besides these banks are subject to periodical examination by the bank examiners specially appointed by the Comptroller of Currency. The National Bank Act requires the submission of five reports of their banking operations during the course of a single year. The Controller of Currency is invested with general supervising power over the banks and the charter of incorporation of each bank is to be renewed once in 20

* The various National Banks in the different American cities are divided into three classes : (*a*) National Banks in the Central Reserve Cities (Chicago, New York and St. Louis) have to keep 25 per cent. Cash Reserve in lawful money. (*b*) Reserve City Banks (about 50 National Banks situated in towns whose population was not less than 50,000 inhabitants) must keep 25 per cent. but half of it may be deposited with National Banks in the Central Reserve Cities, (*c*) National Banks of third class have to keep 15 per cent. of Cash Reserve and of this 3/5 can be deposited with the National Banks of Reserve Cities. These rigid reserve requirements of 1863 National Banking Act have been modified to a great extent by the Federal Reserve system introduced by the F. R. Banking Act of 1913. The proportion was fixed at 18 per cent. instead of 25 per cent. in Central Reserve Cities, 15 instead of 25 in reserve cities, and 12 instead of 15 elsewhere. Only one-third of the Reserve was to be in cash and the remainder could be deposited with the Federal Reserve Bank. This Act was amended in 1917. The whole reserve was to be on deposit with the Federal Bank, the cash held was left to unfettered discretion and the proportions are reduced to 13, 10 and 7 per cent. Only 3 per cent. Reserve is required against time deposits while previously 5 per cent. Reserve had to be kept.

This peculiar law about the Reserve helped the process of financial domination of Wall Street over the country. The National Banks are permitted by the law to keep their reserves outside and the New York Bankers absorbed these deposits to a great extent and utilised them in financing the dabblers of the stock exchange. But the Federal Reserve Act has brought about the needed financial decentralisation.

years. The Indian readers will no doubt be staggered at the vast output of this banking legislation.

In England, the home of the laissez-faire theory, similar supervision has never been designed nor would have been tolerated by the banks. The Bank Charter Act of 1844 still governs the working of the Bank of England and its note issue. The other banks are incorporated under the various Company Laws and beyond this there is no special legislation as regards banking business in England. English Banking has evolved on the principle of " Every man for himself "* while other Governments have considered it wise to throw their shield around every bank. According to Mr. Hartley Withers " it is not good laws but good bankers that produce sound banking."

While the English Economists and bankers object to a normal amount of control, help or interference on the part of the government it must not be construed as an aversion to State help during abnormal times. They incline to the opinion that the Government should stand " behind the banks " and protect them on emergent occasions, whenever a crisis appears, the Bank of England is expected to increase the note issue and give ease to all the sound institutions by providing them with note currency. The quasi-legal understanding in the British community is that the Bank Charter Act of 1844 will be suspended in all times of grave anxiety.

During the period of the late war new measures

* G. H. Pownall's inaugural address as President of the Institute of Bankers—1916.

had to be adopted to save the situation in almost all countries. In England steps had to be taken to protect the banks, acceptance houses, bill brokers and stock brokers. In short the whole money market had to be supported. Such was the paralysis with which business was affected. Neither the usual method of suspending the cash payment as in 1810-20 nor the suspension of the Bank Act of 1844 as in 1847, 1858, and 1866, would alone have saved the situation.*

The Dominion of Canada has only eighteen Chartered Banks but has four thousand branches and the official regulation of banking by the Federal Parliament is a noteworthy feature. The Canadian Bankers' Association supervises the issue of notes and reports to government all over-issues and takes charge of suspended banks. Each Chartered Bank is a member and its quarterly journal is of an excellent quality. Banking is a real profession there with its own policies and traditions and the trained banking officers have a thorough grasp of the credit situation. In spite of these facts the Canadian Federal Parliament revises decennially† the Charters of the banks which are liable to amendment at any time in the interests of safety and public convenience. The most recent instance that can be quoted of its anxiety to safeguard public interest is the passing of the Federal Farm Loan Act, thus designing

* For a description of the crisis the "War and the Lombard Street" of Mr. Hartley Withers can be consulted and for the various measures adopted an authoritative account can be obtained from A. W. Kirkaldy's—British War Finance.

† The next decennial revision will take place in 1933.

separate machinery for the helping of the Canadian Farmers with long-term credits * needed for their agricultural improvement.

The Government of India follows the footsteps of the Government of the United Kingdom. The English Bankers that is the founders of the Agency Houses † taught Joint Stock Banking business to the Indian community. As Prof. Dicey says "the Englishmen carry their common law with them wherever they go" and English Bankers in India can hardly be expected to be more docile in submission to banking laws. As a result of this fact general banking laws regulating banking business are few in India.

The Government of India circularised ‡ the various provincial governments inviting suggestions for banking legislation in 1913 but with the advent of the late war the question was practically shelved. The different chambers of commerce were approached and the majority of them inclined favourably towards banking regulation on broad and general lines. From a recent circular § one learns that the government of India wishes to legislate making it compulsory for every Indian Joint Stock Bank to publish monthly its own operations according to an

* *Vide* L. M. Minty's article on the Canadian Federal Farm Loan Act published in the quarterly proceedings of the London School of Economics (1922, October).

† Many of them were Directors of the Bank of Bengal during the days of 1813—29 and effectively shaped its policy.

‡ 22nd Aug., 1913—Letter No. 6905—The Department of Commerce, The Government of India.

§ 17th Nov., 1920—The Department of Commerce and Industries, Letter No. 8071.

approved form of balance sheet. Beyond it, it has declined to proceed further, and its decision is indeed lamentable.

Even China "the home of strife, of flaunted authority, of widespread disintegration and of national penury" is making rapid strides in the matter of her banking business. Before the recent War, banking business was nothing but a pawn-broking profession. The native bankers never helped the Chinese Government for the development of railways, industries, or reorganisation purposes. But with the closing of the foreign markets in the recent war the Chinese Government had to cajole the leading native bankers and quite a profitable business was done by the Pekin Banks in financing the Government at 15 to 20 per cent. rate of interest.

There was then a rush for banking business and various guilds are now financing themselves by starting banking firms of their own. So to-day one finds Silk Banks, Agricultural and Labour Banks. Chinese Banks are established even in foreign countries (*e.g.*, Sino-French Bank, Sino-American Bank, Sino-Italian Bank, Sino-Belgian Bank, Sino-Danish Norwegian Bank). The starting of these banks is having an appreciable influence in bringing about peace, order, and tranquillity. The Chinese Mandarins and medal-bedecked Tuchun are realising the futility of civil war and many of these are undertaking banking business.

These newly started ventures are agitating for legislation to help them and smooth their progress.

The second United Chinese Conference at Tientsin has passed resolutions inviting legislation in the matter of issuing notes, bills and cheques. It wants the abolition of the tael for the dollar. It is pleading for the exemption of transportation fees on all bank notes and specie payments from one bank to another. It points out the necessity of stopping the minting of old silver and copper currency. It is agitating for the recognition of the existing clearing houses and banking associations in the country. It is asking the State to start a bureau of information to ascertain the financial standing of business firms, and just as Dun's and Bradsteet's reports do in America, give them an official rating, or failing this to establish an inquiry bureau such as Stubbs, Seyd and Schimmelpfeng. It requests the State to establish a standard technical terminology for banking business. The foreign bankers' association of Shanghai is closely co-operating with the Chinese banks and an international banking association is to be started shortly.

Although India does not stand so disorganised, bankrupt and in a morass of helplessness as China, the Indian Joint Stock Banks can follow the path shown by their Chinese contemporaries.

Plea for Banking Legislation in India.

Several prominent Indians have suggested legislation for the better management of banking business. Discussion keenly centred round this pivotal point after the failures of the Indian Joint Stock Banks. There is a consensus of opinion in

this matter and the necessity of passing idealistic legislation as a safeguard against a repetition of failures, must be acknowledged by the bankers and recognised by the Indian public.

At present there is little or no banking legislation hardly worth its name. The Government of India has committed the fatal blunder of requiring all companies, banking as well trading concerns to be incorporated under the same act *i.e.*, the J. S. Companies Act of 1913. They have shown a deplorable lack of banking ideals in permitting the authorised capital of a bank to be much larger than its paid-up capital thus tolerating inadequate banking capitalisation. An undue prolongation of the paying in of capital is another short-sighted policy allowed by the government. The paying of dividends out of actual capital or when a substantial reserve has not been accumulated has not been prohibited. The character of bank loans has not been defined. The granting too large a proportion of the loanable funds of a bank to individual borrowers has been permitted. No definite cash reserve is stipulated. The advisability of legislating to get a better security of deposits has not been considered. There is not the least semblance of an independent bank examination on the part of the government or of the clearing house. Not much of publicity is insisted upon.* Only the loans of a bank have to be divided under certain headings and

* The particulars required by the Act of 1913 are given in Form G, Third Schedule, Act of 1913.

information has to be given on this point.* There is no power to call for any special return from the bank.

Reasons for Banking Legislation.

Familiarised with the stable private banking houses of the indigenous bankers the Indian people in the smaller cities and places view the Joint Stock Banks managed by outsiders with some apprehension. The recent failures made them all the more suspicious. Even though there are only a few banks possessing funds larger than Rs. 5 lakhs and a host of smaller concerns there is no reason why our banking regulations should not be stiffened.

General banking laws are required not to provide the proverbial "strait-jacket" for our banks but only to inspire the public with confidence while giving the necessary freedom to our banks to make their business flexible and adaptable to the business needs of the community the general banking laws should forbid them to venture out on other fields than banking.

The Government should take the initiative in this matter. Neither the fewness of our banks, nor the fact that they are managed by trained westerners must stand in the way of official regulation of our banking business. The apathy of the existing Indian Joint Stock Banks is hardly creditable to them. So long as they are doing sound

* The Registrar of the Joint Stock Company has to be furnished with a balance-sheet of the Company annually along with the Register of shareholders :—*Vide* Indian Companies Act of 1913.

business no official regulation hinders them. On the other hand it will help them to a great extent in creating confidence in the minds of the people. Education of the masses as to the utility of the banks and their services is a slow process and it takes several years to create that confidence in the minds of the Indian people. Official regulation will accomplish the same in a shorter time as the Indian people have a touching belief in the potency of official law.

It is true that "there is no legislative road to banking paradise" as one English banker puts it. Legislation may not be the panacea for any of our banking ills. Government control and inspection may not prevent banking failures. It is indeed true that many of the National Banks of the United States of America failed in spite of detailed banking laws* and rigid government control. It is quite likely that the machinery of government will not produce a competent staff to supervise the various banks in an effective manner. It is undoubtedly certain that control emanating from within by the depositors, by the shareholders and by the customers will be more effective and valuable than control from without by Government-appointed examiners.

Good directors, good servants and good auditors can accomplish more than any sort of ideal

* A table relating to National Bank failures enumerating the causes, is quoted by H. G. Moulton in "Money and Banking" (from the Report of the Controller of Currency, 1911, U.S.A.) within the years 1865 to 1911 about 514 National Banks failed.

regulations. However it must be recognised that much benefit will result from sound banking laws. The newly started banks can derive invaluable aid from these restrictions. Some banks finding nothing to hinder them in the shape of laws may become " adventuresome " and tie up the depositors' funds and come to grief. By all means the banks should be progressive and display the pioneer's willingness to turn their hand to whatever comes in their way. They should adapt themselves to the changing requirements of their customers but this does not mean that they should play fast and loose with other peoples' money.

The Government so long as it defines the nature of business that a bank has to do and imposes ordinary restrictions which the banks themselves have to arrive at for the proper conduct of their business should be regarded as doing its legitimate duty and cannot be said to transgress the freedom of bank officials. The Government should see that thrifty people do not suffer by entrusting their savings to bogus banks. Only the Government should not make the banks instruments of its own and incline to the pernicious idea that " the best way of creating money is to borrow it."

Government legislation may be unnecessary in the case of highly advanced countries where the banks themselves understand their legitimate business and where the public are alive to their responsibilities. But in backward countries where banking ideals are not crystallised, legislation is not unnecessary. The banks will be new to their

business; the public ignorant of their duties, and many a pitfall can be avoided by following the straight and simple rules laid down by the Government. It is folly to leave everything in amateur hands to regulate their business by the quantum of their own limited experience or inadequate bye-laws they may pass for themselves.

Government legislation may be unnecessary when all the directors of the banking companies actively participate in the management and framing of their bank policy. But the real fact is that several of the smaller Indian Joint Stock banking companies are working under the well known managing director system and the managing director initiates the policy, carries it out and is mainly responsible for its financial results. The other directors are mere figureheads easily dominated by this personality and though it must be recognised and acknowledged that these managing directors are not of criminal intentions, yet their descent to Avernus is made possible by the absence of strict laws and actually facilitated by the co-directors who do not realise their own responsibilities.

Even in England, the long series of defalcations of clever and astute financiers during recent years—Jabez Balfour, Whitacker Wright, Hooley Farrow, Bottomley and Bevan is drawing the attention of the public to the defects of their company law and public opinion * seems to

* "Manchester Guardian"—Article of the Financial Editor on the Bevan case.

incline to the view that the English company law, relating to the duties of their auditors, the details of information to be published in their balance sheets and the form in which company prospectuses should be published, must be carefully defined and strengthened.

Legislation may defeat its own object or may place troublesome shackles barring the path of the intelligent banker well versed in the soundest traditions of safety and gifted with a long-sighted view of the real requirements of the nation. But unfortunately for India her roll of distinguished bankers is very limited. Except the late George Dickson who originated the amalgamation idea of the three Presidency Banks and the late A. M. Lindsay who foreshadowed the application of the Gold Exchange Standard system to India and who had the adroitness to prophesy that "his scheme will be accepted by the Government in spite of themselves," the rest of the bankers had only chequered ideas and half enlightened notions on the banking needs and requirements of our people. Banking business should no longer be considered as a profit-making, endeavour and the interests of the shareholders should not always predominate. Banks are endowed with the dignified prerogative of creating credit. Not only should they make a sound and proper use of credit but they should prevent as far as it lies within their hands any unfair use or abuse of credit. This prerogative should be exercised for the real benefit of the community leading to a full and wise economy of

precious metals extending production, enlarging manufactures and increasing trade and commerce. National interest and national benefit should be the actuating motives of the Indian Banker.

When again there is no enlightened public opinion to chastise the shortcomings of the bankers or to effectively demand rapid development of sound banking facilities, it is not wise to expect that everything would go on without a hitch.

The Government of India should realise that the real power of the banks is being blindly exerted in the direction of profits to the shareholders alone and that several of the smaller banks which are more numerous than the larger banks are not being controlled calmly by perfect knowledge. This is no insinuation against the present bank managers that they have expanded the quantity of bank credit out of all proportion to the general economic expansion of our country, or that they have built up a huge credit structure on a small basis of gold reserve as is the case with the English banks. The sole contention is that the small banks are too anxious to attract business and they set at naught wise and prudential principles that should govern the supply of credit. For instance the supply of credit for buying fixed capital is discountenanced by all banking experts and financiers but some of the Punjab Banks which failed in the crisis of 1913 to 1915, lent too much money to the cotton-ginning factories and this liberal dispensation of banking credit led to a gross multiplication of these factories out of all proportion to the cotton-producing capacities of the province.

Some of the present banks are evidently anxious to bring about a rapid industrialisation of their provinces, thinking that banking credit alone would enable the raw materials to be successfully manufactured into industrial products. Although credit facilities are sorely needed, it must by no means be concluded that banks should dispense with the following points in the matter of granting credit. The business capacity of the applicant, the prospects of an early repayment of the loan, the general political situation and the reliability and commercial standing of the applicant and lastly the bank's own financial position should be always kept in mind by the bankers. Loans to small traders who are unable to produce good bankable securities and to small manufacturers who cannot show orders from good firms or invoices of goods already sold and ready for despatch are unsound, and these rules never loom large in the minds of the small Joint Stock Banks of this country and as a matter of fact several of these combine trading with banking business. Some of the Bombay banks finance speculators on the Stock Exchange or cotton green or bullion market on a very extensive scale.

Although credit has not been put to any misuse in this country yet the proper husbanding of our credit material and the correct use of it is not to be seen in the case of the small banks. It must be understood by these banks that credit is one of the factors indispensable for increasing the wealth of a country and so long as credit increases the supply of commodities it tends to cancel the tendency for prices

to rise. Hence if the loans and discounts of our banks actually augment the stream of commodities flowing into the hands of the community its actual wealth increases and a right use of the credit is made by the bank. But if our banks succeed in placing credit in those hands who fail to increase production they are rendering a fatal disservice to the community firstly by the misdirection of credit, secondly by raising the purchasing power of money in the hands of the people which tends to raise prices and this tendency towards increasing prices is not counteracted by increased supply of commodities and lastly they are endangering their own financial standing by entrusting their resources to the incapable and undeserving producers to whom no quarter should be extended.

Suggestions for Banking Legislation.

Every western economist of reputation repeats the hackneyed opinion that Indians are prone to the hoarding habit.* The Government of India relies on this opinion but yet takes no effective care to enable the people to divorce this habit. With the exception of this stipulation that the Imperial Bank of India should open hundred branches within five years of its starting and the increase of capital they have insisted upon, which certainly will help their own financial business, they have not taken any

* Only the recent Sir H. B. Smiths's Committee has grasped the truth and it says that India's use of gold as a store of value is justifiable in the absence of saving facilities. It also points out how the use of gold in social ceremonies is sanctioned by tradition and religion.

other worthy measures to effectively counteract the so-called "hoarding habit," if it really prevails among the Indian population. They have not expanded the Savings Banks system.

It is of no use to blame the illiterate people while effective measures are not being taken to wean away the people from this pernicious habit. Neither have they induced the people by allurements to deposit money in the Postal Savings Banks nor have they protected them when the banking companies were inducing them to deposit their money in their vaults. On the other hand, the banks are finding it increasingly difficult to attract deposits from the people, as the Government of India itself is attracting all available savings by paying 5 to 6 per cent. rate of interest for all its loans and treasury bills it raises in the money market. Sir Dorab Tata referred to this* fact and complains of the impossibility of the Industrial Banks ever hoping to pay such high rates to their depositors in the expectation that a still higher rate can be realised from the industrialists.

If the attitude of the Government of India towards banking business in normal times is hardly

* Owing to the inadvisability of conducting industrial financing with money borrowed at a high rate the Tata Industrial Bank has transferred its industrial business to a private concern "Indian Industrial Finances" Ltd. Sir Dorab Tata says "The Directors have decided to do no more industrial business for the present. What led them to this decision was that the rate of interest which the Government were prepared to pay for loan and treasury bills coupled with their continued necessity for keeping in the market will militate against any industrial bank obtaining necessary funds for industrial business." Since the above was written the Tata Industrial Bank has been amalgamated with the Central Bank of India.

inspiring; their attitude in abnormal times is hardly worth mentioning. In Canada and the United States of America the Federal Governments undertake the duty of converting the notes of a failed bank and this government guarantee is a virtual protection against their depreciation. Their general understanding is that the Government is "behind the banks." In India, however there is a vague responsibility according to Mr. J. M. Keynes* lying on the shoulders of the Government of India to come to the rescue of the banking system in the event of a widespread failure. When the clock of banking progress received a rude check in the crisis of 1913 to 1915 very little was done to alleviate the situation. In future, at least, the Government should undertake the task of resuscitating and reviving the business of sound banks when they meet with any calamity.† In order to better perform this task the Government should introduce some Government control by legislation, inspection or other means even during normal times. The Government of India should only remember the adage that "It is never too late to mend." Its recent decision ‡ to postpone legislation should be revoked as early as possible and it would be highly expedient

* J. M. Keynes—Memorandum on State Bank appended to the final Report of the Chamberlain Commission.

† It is a matter of gratification to note that the Imperial Bank Act is to be amended with the special object of empowering it to grant help to the depositors of the Indian Banks as they have done in the case of the Alliance Bank of Simla at the initiative of the Government.

‡ Letter of the Department of Commerce and Industries 17th Nov., 1920 (Letter No. 8071).

if it bears in mind the suggestions outlined below. To expect the nation "to work out its own banking salvation by means of its own experiments and its own experiences is unwise economic statesmanship.*

The word "Bank" should be restricted in its application only to those financial companies which undertake to meet all obligations "on demand" and subject themselves to be drawn upon by means of cheques. It should be denied to bogus and unsound companies with a large inflated nominal capital whose sole desire is to exploit the public under the patronym of the word "bank." It is indeed difficult to define the word "bank" and banking legislation should not be extended to those indigenous bankers who do not burden themselves with others' money to such an extent as joint stock banking companies do.

In the matter of the banking companies the authorised capital should never be allowed to be higher than 4 to 6 times the paid-up capital. It would not be unwise if the Government of India also sets a minimum limit to the banking capital which should be declared necessary for a certain amount of population taking into due consideration the character of their business and their demand for credit. If an adequate amount of capital is to be had from the beginning all temptation to tout for business would be removed. It would also be wise on the part of the Government of India to stipulate

* Sir James (now Lord) Meston refused to consider the question of banking legislation on this pedantic plea.

that of the subscribed capital half should be paid up at the starting of the banking companies actual operations and provision should be made that a substantial part of the balance should be paid within six months of the registration of the banking company. Much benefit would also accrue if permission is denied to the banking companies to parade the amount of their "authorised" capital in their balance sheets. Only the subscribed capital and the paid-up capital should be published and if any amount of reserve liability is attached to the bank share, it should also be published. Otherwise the fact that it is a fully paid bank share should be mentioned. No real benefit can be reaped by publishing the "authorised capital" of the bank. The ignorant public who do not very often possess correct notions as to the real difference that exists between the three items, are apt to be led astray by these figures. If permission is given to publish these various items all of them should be printed in the same attractive type.

The Government of India should compel the banks to build up a decent reserve by setting aside a part say 1/10 of the annual net earnings of the banks, till the Reserve Fund amounts to half of the paid-up capital and then only should the banks be permitted to distribute the whole of their earnings as dividends to the shareholders. The law should also aim at prohibiting the banks paying dividends when substantial reserves have not been earned or when bad debts have not been completely written off. It should also be the aim of the law to see that

if the Reserve Fund is invested in securities only gilt-edged securities should be selected for this investment.

The law should permit the banks to lend money to their directors only on the strength of securities and not its own bank shares and at such rates as are charged to the other customers of the bank. The law should make it compulsory that if the directors or industrial companies in which those directors are interested apply for loans, they should not be permitted to attend the Board of Directors' meeting lest their presence may induce the other directors to vote for the loan. The banking company should be prohibited to grant money to its customers on its own bank shares and upon other bank shares if a large portion of them is unpaid. Loaning on real estate should be prohibited but the bank may be permitted to entertain real estate in the event of the depreciation of the original security tendered as cover for the loan.

The law should restrict the amount of loanable money to individual borrowers, to the limit of 25 per cent. of the capital of the bank and if more advances are to be granted, they should only be granted on actual consignments taking care to hold the bills of exchange and its attendant documents as security or on the actual deposit of recognised trust securities accompanied with a letter of hypothecation.

The law should be wise enough to restrict the banks from having too large a holding of one kind of security even though it be a Government security

and the banks should be permitted to invest their money in trust securities and as industrial securities are purely of a speculative character there should be an attempt to prohibit the commercial banks from holding too many of such industrial securities.

The rate of interest from these investments should not be lower than what is actually paid for money borrowed, and as all such investments are unsound finance the banking companies should not be permitted to indulge too much in them.

It has too often been noticed that our small banking companies combine trading and other functions along with legitimate banking operations which are bll discounting, loaning and attracting of deposits. The law should prevent such a combination and the Registrar of Joint Stock Companies should be empowered to delete from the memorandum and articles of the banking company all clauses that may be considered as running counter to the interests of the public or it should be restricted from performing functions as are not usually conducted by banking companies elsewhere. To prevent the Registrar from being the final arbiter in all such cases, appeal should be allowed to the judicial authorities in all matters of doubtful decision.

There is an urgent necessity for the tightening of the criminal law making the directors, the managers and the auditors of the banking company personally liable for deliberate fraud practised on the company or a wilful and a deliberately fraudulent maladministration of the banking funds. Those auditors who certify the different balance sheets

negligently or knowingly as in most cases, that everything is correct, should be taken to task and the auditors, section 145 (2) of the Indian Companies Act must be reformed and heavier penalties imposed in all these cases.

It has become the common practice prevalent among the Indian Joint Stock Banking companies to attach a branch for a savings bank business to their ordinary operations. In all such cases, the law should compel the banks to invest half of this sum secured in the savings bank business, in securities approved by the Indian Trust Act and these should be earmarked for that purpose. The savings bank business, if properly developed, will help to create a banking habit in India.

In accordance with form G.111 schedule of the Indian Companies Act every banking company incorporated under this act shall publish details of its business operations. But this form is not at all a detailed one.

The particular items of the different banking operations should be amplified and set out in greater detail. A frequent publication of such a balance sheet will secure the confidence of the depositors and the general public who may like to transact dealings with banking institutions. Such publicity will go a long way in restricting the scope of the bank and prevent it from undertaking injudicious transactions.

The intention of the Government of India to make it compulsory on the part of the banks to publish monthly statements of business amplifying the necessary particulars that are to be published its

to be hailed as a welcome measure and their intention to secure the interest of the depositors is a noteworthy one. They have adopted the set form originally approved by the Lord Cunliffe Committee and all Indian Joint Stock Banks will be forced to publish their monthly balance sheets as soon as the necessary alteration takes place in the existing law. This form is as follows :—

LIABILITIES.	ASSETS.
. Authorised capital (Shares of Rs. each)	1. Cash in hand (Coins and Currency notes) and balances with the Imperial Bank of India.
2. Subscribed	2. Balances with other Banks.
	3. Bullion in transit and hand.
3. Paid-up	4. Money at call and at not more than seven days' notice.
4. Reserve Fund	5. Indian and British Government securities maturing within 12 months.
5. Current, Deposit and other accounts.	6. Inland bills.
	7. Foreign bills.
6. •Loans against securities as per contra.	8. Balances abroad.
	9. Investments.
	10. Loans and advances.
7. Acceptances on behalf of customers.	11. Other Assets.
	12. Bank premises.
8. Endorsements, guarantees and other obligations.	13. Liabilities of customers for acceptances.
	14. Liabilities of customers for endorsements, guarantees, etc.

There is no gainsaying of the fact that this balance-sheet is infinitely better than the existing one that has to be published along with the annual summary which a Banking company working under the Indian companies act of 1913, has to forward

to the Registrar of the Joint Stock companies. However it would be better if the following suggestions are also accepted and an improvement made in the above form.

(1) The "authorised" and "subscribed" capital need not be published at the head of the liabilities column. An asterisk should be placed opposite the paid-up "capital" item and as an explanation of this asterisk these details should be given in a footnote.

(2) The word "Loans" against securities refers to the borrowings of the Bank and the word "borrowings" should be substituted for loans.

(3) The item "Loans and advances" should be divided under suitable headings as given below. Such a rational division is insisted upon by the Baroda Government and if all Banking companies have to subdivide their loans and advances as follows, it would enable the public to ascertain the stability of the Bank, for the art of Banking wholly lies in successful loaning on reliable securities:

(*a*) Loans secured by the personal guarantee of two or more persons besides the actual indemnity of the borrower. Under this heading come the well-known "Cash Credits" of our Banks.

(*b*) Loans on the consignment of bills as security.

(*c*) Loans resulting from an Overdraft arrangement.

(*d*) Loans granted to Directors and officers of the Bank.

(*e*) Loans granted to Joint Stock Companies on Securities.

(*f*) Loans granted on Joint and several Promissory Notes.

(*g*) Loans considered as doubtful accounts.

(4) The nature of the different investments should be specified in detail as follows:

(*a*) Securities of or guaranteed by the British and Indian Governments.

(*b*) Colonial and foreign government securities.

(*c*) Other Indian Trust Securities.

(*d*) Shares and Debentures of Indian Joint Stock Companies doing Industrial business.

(*e*) Other Investments.

There is no use of bare laws being passed but an efficient machinery to secure their proper observance by the different banking institutions should be created by the Government. The Government of India should have a separate department to inspect the banks or appoint officers of the Indian audit department to carry on an independent audit of the banking work, not merely to supplement the work of the auditors appointed by the shareholders but to make effective suggestions as regards the actual work that is done. The report of the surprise audit should be in duplicate and one of them should be sent to the Registrar of the Joint Stock Companies and the other should be sent to the Board of Directors.

The sole reason why reliance is placed on the government audit is this. The present knowledge of the auditors is very meagre and the majority of them possess no extensive knowledge of the banking machinery. Several of them wilfully and knowingly permit the managers to indulge in unsound finance thus imperilling the financial stability of the institution. The Government audit will not be open to this grave defect and as the report is not thrown open to the public no damage to the credit of the bank can be inflicted by any suggestions the government auditor can make. It is for the board of directors to loyally adopt all their suggestions and

bring about a better and scientific management of the banking institution than before.

It may appear a ludicrous inconsistency if no regulations are outlined with reference to the holding of the cash reserve of the banking companies specially after what has been written before under the heading "The Rationale of Banking Legislation." The omission of any laws as regards the cash reserve is justifiable if the other banking operations are conducted according to the regulations outlined here. Such a wise transaction of the other banking operations will render unnecessary a large cash reserve and if the assets chosen are liquid and easily realisable with minimum of loss to the banker a smaller cash reserve will be found sufficient. Although a legal regulation of the cash reserve can be easily justified on principle yet it can be better regulated if the hands of the bankers are unfettered in this direction. If mutual help is forthcoming as the result of an *esprit de corps* prevalent among the bankers it will enable the bank to pull through an emergency except that of a concerted "run" and in the event of such an unforeseen contingency no amount of cash reserve will be likely to prove sufficient.

The treatment accorded to the immigrant banks is a very fair one and the Government of India wisely abstained from raising a Chinese Wall and refusing access to foreign institutions. This has led to the investing of foreign capital in our country. The exchange banks express their unwillingness to subject themselves to any banking laws that may be

passed by the government and they are unwilling to publish any monthly balance sheet according to the proposed form.

In justice it must be admitted that they never transgress the established maxims of sound banking nor are they inadequately capitalised. Their capital is being employed here as well as in their country of origin and it cannot be ascertained with any degree of accuracy nor is it safe to publish the ascertained amount of capital they employ here and at home. So long as they keep adequate balances for their Indian deposits, that is, deposits attracted in India there is no reason why they should be subject to the statutory rules that may be enacted here. Just as the indigenous bankers are to be exempt from the application of these laws similarly these immigrant banks should be accorded quite a separate treatment from the Indian Joint Stock Banks but favouritism should not extend further.*

Other Suggestions.

The Indian Joint Stock Banks should play a more useful part in the financing of the internal trade of India. The charges for inland remittance should be reduced to as low a figure as possible. Instead of financing the speculative investors who dabble on the stock exchange they should extend their business into the interior of the country. Thereby they would not only be "popularising" banking business

* Formerly the Indian exchange banks used to get deposits from the Secretary of State for India out of the London cash balances at very cheap rates of interest.

but they would standardise the inland instruments of exchange, *i.e.*, the hundies and inculcate business-like habits in the minds of its customers.

TABLE SHOWING THE GROWTH OF THE BUSINESS OF THE INDIAN JOINT STOCK BANKS.

(Banks with capital and reserve above Rs. 5 lakhs and over).

Year	No. of Banks	Paid up Capital Rs. (1000)	Reserve	Total	Deposits	Cash balances.
1870	2	983	182	1,165	1,395	507
1880	3	1,800	311	2,111	6,337	1,663
1890	5	3,550	1,759	5,109	27,078	5,579
1900	9	8,212	4,560	12,772	80,752	11,904
1905	9	8,457	7,782	16,239	1,19,892	17,350
1910	16	27,556	10,055	37,621	2,56,585	28,025
1913	18	23,133	13,294	36,427	2,25,919	40,017
1915	20	28,139	15,665	43,804	1,78,727	39,941
1916	20	28,736	17,366	46,102	2,47,105	60,349
1917	18	30,370	16,299	46,669	3,11,701	76,484
1918	19	43,645	16,559	60,204	4,05,948	94,858
1919	18	53,907	22,427	76,334	5,89,947	1,21,663
1920	25	83,702	25,546	1,09,248	7,11,464	1,63,070
1921	27	93,880	30,081	1,23,961	7,68,993	1,56,590
1922	27	80,224	26,165	1,06,389	6,16,386	1,20,388
(Banks with capital and reserve between Re. 1 and 5 lakhs).						
1913	23	3,914	1,135	5,049	15,115	2,495
1914	25	4,222	1,302	5,524	12,654	2,799
1915	25	4,538	973	5,511	9,137	2,001
1916	28	5,177	1,150	6,327	10,123	1,676
1917	25	4,416	1,024	5,440	9,920	2,042
1918	28	4,865	1,443	6,368	15,535	3,690
1919	29	5,311	2,186	7,497	22,849	5,371
1920	33	6,142	1,995	8,137	23,346	4,191
1921	38	7,705	2,323	10,028	32,602	4,352
1922	41	8,300	2,765	11,065	33,789	5,602

Explanation :—The points that should be noticed are (1) the fall off in the deposits after 1913-15 crisis, (2) the small amount of cash balances held against deposits in 1913-15. Till 1917 no satisfactory cash balances were maintained. The position is more glaring in the case of the smaller banks.

CHAPTER V.

THE INDIGENOUS BANKER OF INDIA.

The term " banks " and " bankers " are quite modern but the profession is an old and time-honoured one. The word " banck " was a German term signifying a joint stock fund. The Italians used the word " banco " meaning a heap of money or an accumulation of stock. The common derivation of the word " bank " from the counter upon which the Italian money changer used to lay out his stock has been ridiculed by H. D. MacLeod on the ground that the " Italian money changers as such were never called ' bancheiri ' in the middle ages." * Whatever might be the origin of the word " bank " we see that the etymology of the word bank suggests an origin which would trace the history of banking in Europe from the middle ages.

The Meaning of Banking.

Originally banking has had its origin in the efforts of individuals to supply certain primitive wants of an advancing community, namely, lending and receiving deposits. The process of satisfying these wants was by means of a few perfectly simple operations. But with the evolution of time these individual wants sank into insignificance and the unforeseen, much disputed

* H. D. MacLeod " Theory of Credit "—Volume I, page 90.

and ulterior effects of a banking system have been recognised. The primary and original functions of banking namely lending and receiving deposits are still the more important functions but a great variety of services are performed by modern banks and with the advent of specialisation due to the progress of society we find a diversity of banking operations, as well as institutions. It has fallen to their lot to finance industries, to liquidate the international indebtedness, to manipulate the currency system and lastly to mobilise credit.

H. D. MacLeod says that the meaning of the word " bank " is " to issue credit."*

C. A. Conant describes the banker as " a trustee of the money of the depositors," and as " the trustee of the mechanism of credit for the entire community."†

Gilbart ‡ lays down the following banking functions " provision of safety deposit vaults payment of interest on deposits, making of loans, exchange of funds between places, changing of currency denomination, collection of notes and drafts." In his opinion " the banker should gather money in small sums and transfer it in larger amounts to borrowers engaged in trade and commerce."

According to Dunbar the three functions of a banker are deposit, discount, and issue. While the " banker creates no new wealth by his lending and

* H. D. MacLeod " Elements of Banking."

† C. A. Conant—Principles of Modern Banking—Volume II.

‡ Gilbart—Principles of Banking, Michies version, pp. 213-222.

deposit holding; he directs the existing capital to the enterprises and industries most in need of support and quickens the succession of commercial and industrial operations."*

Horace White defines a "bank as a manufactory of credit and a machine for facilitating exchanges." He defines the discounting function of a banker as "the swapping of well known credit for less known credit. He adds that the banker enables the most deserving persons in the community to get capital," and performs "a service to society by economising tools and materials."†

Holdsworth ‡ says that "commercial banks receive deposits of cash, cheques, drafts, and make loans to the business public by discounting or purchasing commercial paper. It also provides a medium of exchange to the issue of circulating notes. Speaking of the commercial banks as a manufactory of credit he says that business credit cannot be conveniently used for current business transactions but bank credit in the form of cheques and drafts is widely acceptable.

H. P. Willis says "the dominant function of a bank is that of guaranteeing the limited or individual credit of each individual by accepting and substituting in lieu thereof the bank's own secured note for example to a bank and discounts it and then draws cheques against his account at the bank

* Dunbar—History and Theory of Banking.

† Horace White—Money and Banking.

‡ Holdsworth—Money and Banking, pp. 148-149.

and he has simply substituted the bank's credit of more general acceptability for his own credit of limited acceptability." "In his opinion the bank is an institution for the study of credit and for guaranteeing its judgment on that subject." *

Scott writes that the "customers of a commercial bank sell to it their surplus cash and credit instruments representing payments due to them from other persons and make loans from it secured by their personal notes due to them as a result of their transactions. They are credited on the books of the bank in a form known as deposits. The making of loans and discounts is a function correlative with that of conducting deposit accounts. It may be described as a process of advancing funds on the security of personal notes." †

J. L. Laughlin says "the business of a bank consists of dealing in the commercial paper which grows out of current transactions. When a man desires funds for a long period he should get them not from the bank, but from those who have spare capital to invest for some considerable period of time. The bulk of banking business consists of instruments evidencing claims upon individuals, stated in terms of money and resulting from operations requiring a comparatively short period for their consummation." ‡

G. D. Chisholm in his article on scientific banking says "The banker is the trustee of the

* H. P. Willis—American Banking—pages 3 to 4.

† W. R. Scott—Money and Banking—pages 108-109.

‡ Laughlin—Banking Reform.

nation's security. He is the trustee of nation's material future."*

From a simple dealer and broker in money the banker has become the arbiter of a nation's industrial organisation and even of "the fate of nation's" as Conant says.†

The Development of Banking in Europe.

According to Conant the forerunners of modern bankers were "the individual money-changers, the Jewish money-lenders and the Lombard bankers." ‡ As industry expanded by leaps and bounds and as centralised government emerged out of the welter of political chaos and a national life became organised the necessity for public banks arose. The Bank of Amsterdam was organised to remedy the defects in the currency circulation of Holland. The Bank of England would not have come into existence so soon but for the necessity to finance the Dutch Wars of William III king of England. So European banking understood in its modern sense is barely three centuries old. But India on the other hand had a widespread banking organisation some centuries before the modern term "bank" has been coined.

The Origin of Banking in India.

Evidence is forthcoming in abundance that the business of banking was perfectly understood by the people of ancient India and fairly practised by them. Dr. Pramathanath Banerjea quotes from

* Chisholm—Journal of the Institute of Bankers—London, 1918.

† C. A. Conant—History of Modern Banks of Issue.

‡ Conant—Principles of Money and Banking, volume II.

Gautama, Brihaspati and Baudhayana verses which regulate the rate of interest.* The institutes of Manu give us rules regarding the regulation of interest and the policy of loans.† Kautilya has some advice on these points ‡ Sir W. W. Hunter gives us valuable information as to the manner in which a private banker sets up his business.§ Some glimpses of the indigenous system of banking can be obtained from Mr. Malabari's account.|| Sir Richard Temple testifies to the fact that "banking business was carried on by our ancients. He estimates the number of bankers to be one hundred and eighteen thousand adult males of which some are money-changers. There are half a million of villages and there are about two bankers—to every village."¶ The 1921 Census of India estimates "the number of bankers to be about 1,461,000 but it includes bank managers, money lenders, exchange and insurance agents and money changers."** Dr. R. Mukherjee †† cities literary and epigraphic

* Dr. P. Banerjee—Public Administration of Ancient India.

† Burnell and Hopkins—Ordinances of Manu.

‡ Kautilya's—Arthasastra.

§ Sir W. W. Hunter—Imperial Gazetteer of India, Vol. IV.

|| *Vide* his "Guzerat and the Guzeratis."

¶ Sir R. Temple's lecture before the Institute of Bankers. Journal of the Institute of Bankers, Volume II, 1881.

** "Banks and money lenders numbed 4 per mille in the total population or twice as plentiful in the Punjab, their number exceeds the general average in Bombay, the Central Provinces and Berar and is somewhat below it in Bengal, Madras and the United Provinces while in Assam it is only 1 per mille,"--*vide* Census of India, 1921, Volume I, chapter on occupation. The previous estimates in 1901 and 1911 Census are 1,156,000 and 1,128,000 respectively.

†† Dr. R. Mukherjee—Local Government in Ancient India.

evidence as regards the prevalence of banking in ancient India.

But no connected historical account of our Indigenous banking system has ever been written due to the paucity of materials. Secondly no statistical information has been collected by our previous rulers. Thirdly the lack of political tranquility for a number of years must undoubtedly have told very seriously on the banking houses. Lastly the bankers, plied another occupation notably that of a merchant. A Banker *quâ* banker did not exist in the past. He is something more than a mere banker. Strictly speaking there are no indigenous bankers in India. What everybody calls bankers are either money lenders lending upon landed security or other property or agricultural produce and also in industrial products.

Many of the indigenous bankers held high political authority at the Moghul Courts and the advent of the British rule has no doubt destroyed their political importance and prestige. The political influence of Jagat Seth * and Omachand, during the Plassy days is well-known to students of history. The Seths of Madura exerted much influence on the political history of South India. History has

* A brief history of the house of Jagath Seth—The founder of the house was a marwari rajput who immigrated from Jodhpur somewhere about 1695 and settled in Patna and began money lending business. His seven sons migrated to different parts of Bengal. The eldest son Manik Chand migrated to Dacca and became the court financier of the Diwan Murshid Kuli Khan the founder of the house of Murshidabad and to whom was entrusted the task of remitting Bengal's contribution to Imperial Delhi. In 1715 he was given the title of Seth and his adopted son 'Fatehchand' was given the hereditary

recorded that these bankers financed the wars of the petty princes and granted loans to their principalities.* The indigenous banker continued his avocation undisturbed during the times of the East India

title of "Jagath Seth" or the "banker of the world" by the then Emperor Mohomed Shah. In the year 1742 they felt the first stroke of ill-luck when a Maharatha horde—part of Bhonsley's defeated army at Burdwan—swooped down on the house of Jagath Seth and carried away two crores of rupees. In spite of this loss they carried on their banking business and in 1747 they lent the English 12 lakhs of rupees. From this period their influence is to be noticed in the affairs of the British in Bengal. Nawab Surajdaula on account of his cruelty and injustice soon became unpopular and fell out with his banker the Jagath Seth who refused to raise three crores of rupees from the European Merchants. His openly insulting him in the Durbar led to the latter's intrigue with the English Officers of the East India Company. It was in the house of Jagath Seth that Watts, Walsh and Schrafton met with the ill fated Umichand to work out the details of the plot by which Mir Jafar hoped to obtain the subaship of Bengal. The Jagath Seths continued to flourish under the new Nawab and their relations with the English became more friendly. When Jagath Seth visited Calcutta in 1759 the English entertained him at a cost of Rs. 12,000.

When Mirkasim came to the musnud he did not tolerate the friendship with the English and after the recapture of Patna from Mr. Ellis he drove every Englishman out of his dominion and conveyed the bankers to Monghyr. When he was completely defeated by the English at Jheria he got his European prisoners shot down by his soldiery. Ranmarayan of Dacca was cast into the river, Raja Rajbulub was put to death with all his sons and after draining away the wealth of Jagath Seth he ordered him to be thrown into the Ganges from one of the bastions of the Monghyr fort. In spite of the survival of a few connections here and there, the house of the Jagath Seths decayed until there now remain but the ruins of the beautiful Jain and Hindu temples of marble and porcelain, the old Indian mint and the mere skull of that once princely dwelling of these bankers in the vicinity of Mohimpur near Murshidabad the capital of the Nawabs of Bengal.

* The Nagerseths of Bengal financed the local Nawabs. The Peshwas of Poona were financed by these bankers. One Banslal Abechand financed the Government of Bengal during the days of the Great Sepoy Mutiny of 1857.

Company and although deprived of his political importance he was playing no mean rôle in financing the internal trade of India. It might be quite true that the pristine honesty and scrupulous regard for truth which were some of the salient features of the ancient indigenous banker, might have been dimmed by the more materialistic tendencies that have been introduced of late into the calm and placid atmospheres of our social life. Either this fact or "the passing of the English law of bankruptcy has demoralised the native bankers in the presidency towns."*

Many of the indigenous bankers might have disappeared or fallen into ignominy but the business itself is still being carried on, on the same old lines as before. The joint stock banks, the branches of exchange banks, the Imperial Bank of India and the new born Co-operative Credit Societies whose number is legion have all invaded their sacred precincts and are seriously competing with them for business but they are holding their own limited business though in a less restricted sphere than before. Come what may, they do their business in the old traditional manner and show no signs of adapting their business to the altered circumstances of the present day. Solidity of business is no doubt a prominent feature of the indigenous banking houses but they are lacking in adaptability and initiative which characteristics also, a sound banking system should possess.

* Sir Richard Temple, "Journal of the Institute of the Bankers," 1881.

Several Names.

The indigenous bankers of India are known by several names in the different parts of India. The most common names are Saucar, Bania, Chetty, Mahajan, and Shroff. The well known indigenous banker has almost become an indispensable figure in our social organisation. He is not only to be met with in the presidency towns where he goes under the appellation of "shroffs" but even in obscure villages far off from the abode of civilisation. Here he is known as the 'Bania' or Saukar.

The business of the indigenous banker is purely a family concern and hereditary in the family. So banking business in India is usually conducted by a class or caste. The father of the family is a banker. He transmits the knowledge and good will of his business to his son and so on. So the class has not been strengthened by the infusion of fresh blood into it.

No new ideals take hold of the business man. His conservatism is of course a strong asset and saves him from many a bad debt. He is more a private capitalist owning magnificient sums.* They are generally averse to the principle of Joint Stock Banking. In many of the towns they form private partnerships managed by the senior partner. They seldom reveal their transactions to the public. They are most courteous and indulge in gossiping. They entertain you on a variety of

* A close scrutiny of the list of the subscribers to the Indian War Loans, will reveal the princely sums that have been invested in them by these individual bankers.

topics but they set a seal on their lips as the drift of conversation turns to the extent and magnitude and other facts relating to their business.

But the one great distinction is that this private bank is always in the hands of one family. A man who originally starts a private bank may be a good banker, financier and business man but it does not always follow that his son, who in all likelihood and certainly inherits this business, will be capable of running it. The private bank wants continuity of family. It wants continuity of young men coming on who are willing to work and who have the ability to work successfully. It is difficult to find that all these factors are satisfactorily obtained in a private bank. The efficiency and driving power which are to be found in Joint Stock Banks are seldom visible in these private banks. The Joint Stock Banks do not go from father to son but are always under efficient and capable management. This is one feature that is telling heavily against the indigenous bankers and their firms. The verdict of history has gone against them especially in England and western countries but the indigenous banker of India has still enough scope to pursue his business. A grave and serious warning has been given that they have outlived their period of usefulness.

Some of the big indigenous bankers * have their

* The Village Saukar who is more a lender of money than any thing else, keeps no accounts and the Marwari Saukars keep a memorandum book in which they keep their accounts. But there is no elaborate system of book-keeping in this case also.

agents at all the important trade centres of the interior. These agents or "gumastas" are sometimes called "moonims." These are oftentimes changed from centre to centre in order to enable them to understand the local conditions of these several places and when once the agent is made permanent he serves the employer the whole of his time and devotes his whole energy to the success of his firm. Although the pay given generally ranges from Rs. 30 to 60 a month, dishonesty on the part of these officials is of rare occurrence. These send weekly accounts of their work to their head office and occasionally receive instructions from the head office. Their books and accounts are written in the local vernaculars and they are carefully audited by the indigenous banker himself. This personal supervision goes a long way in preventing fraud on the part of the officials and it also gives a close mastery of facts and figures relative to the business.

Every year on the "Deepavali" day, they worship their books and distribute alms to the deserving on that particular day on a most lavishing scale. The Brahmins are fed with sweet-meats and other delicious dishes and given a handsome Dakshina or present on this New Year's Day for them. The new account books are placed on the same pedestal as the Goddess "Varalakshimi" and worshipped. Some of the indigenous bankers set aside a small moiety of their gains in a small charity box on each and every item of profitable business. In the big cities where a number of these bankers transact business these gains are collected

and their general association * determines the best manner in which it is to be spent. They are well aware of the dictum that " charity begins at home," but are not forgetful of the saving clause that " it does not end there."

Functions of the Indigenous Banker.

The indigenous banker is a dealer and broker in capital. His main business is to lend money. It is not purely a case of personal security that he likes but the indigenous banker is the most inquisitive of all mankind and the customer has to give him his free confidence. Since the loans are generally for performing social functions or other unproductive purposes he takes good care to take collateral securities to balance the amount of his loan. He deducts interest beforehand and pays the outstanding balance to the customer. He takes care to collect the debts by monthly instalments. His rate of interest is often so high and he is so exacting in his terms that he had been termed the " Indian Shylock." But there has been a marked fall in the rate of interest due to competition from the co-operative credit societies and the increase of stability

* Even in the matter of helping poor and deserving people one prominent member of the association heads the subscription list and passes it along to other members, and each member contributes his own quota. The common realisation of their aims, their solidarity of interest, their spirit of mutual help and co-operation are all noteworthy features. The Indian Joint Stock Banks have no association of their own. The existence of such an association would teach them all these necessary qualities that conduce for success in their business.

and security due to the British rule. The high rate of the rural banker is due to the worthless security of the ryots on the one hand and the difficulty of collecting has also to be reckoned by him.

Again the financing of agriculture which is largely dependent on monsoon and which is only a seasonal occupation means half-time occupation for money and so it has to earn a high rate of interest when it is employed.* He supplies capital in small doses and protects the ryot from the rapacious hands of the landlord. Thanks to the co-operative credit societies the predominance of the rural banker is fast decaying and he is daily losing his ground. As Mr. Wolfe remarks "Co-operation has brought money to many a spot thirsting for it, replaced hopeless insolvency by solvency, liberated many from the usurer's yoke and awoke many a mahajan or saukar to find the fact that his occupation is gone." 'As the co-operative societies are gathering strength and are beginning to work successfully, the mahajan himself is drawn into the vortex of the society. He supplies the capital as he finds better security and no risk when he lends to the co-operative society. The co-operation of the mahajan is to be enlisted because he is the only educated person

* This is no attempt to vindicate the usefulness of the village Mahajan. Sir T. Morison has proved that his existence is clearly a benefit to the Indian ryot. Sir D. Ibbetson and Dr. R. Mukherjee have each a good word to put in for the rural banker.

The defects of this system of agricultural financing will be dealt with in the chapter on Mortgage banks. His shortcomings as an industrial banker will be dealt with in the Chapter on Industrial Banks.

knowing something about banking and if his services are enrolled in the cause of the co-operative movement it will not only result in the elimination of a dangerous competitor and rival but will bring the aid of his expert knowledge to a just cause.

Comparison with the Money-lending Policy of Western Joint Stock Banks.

The Commercial banks of Europe do not grant loans for long periods and lock them up in unrealisable assets. They never forget that all the assets of the bank should be within quick and easy control of the bank. But the indigenous banker does not conform his business to these principles. He lends money on every kind of security preferably land, real estate and jewellery. As the working capital is his own he is not afraid of any run.

Again the European banker weighs each debt by itself. He grants loans on sufficient collateral security placed in his hands and the indigenous banker balances good against bad debts. He distributes his risks among his various clients. When a higher and more tempting rate of interest is offered he willingly hazards the risks but of course he has the prudence to take some kind of security. So the necessity to write off bad debts is less urgent in the case of the European banker, and the native banker though he does not use his capital gets it locked up in real estate or other properties so for sometime at least there is a temporary diminution of capital with which the business is run. The indigenous banker does not understand that " the

banker should be a liveried stable-keeper who must keep his horse always ready for hire." He should realise that "banks are made to make capital circulate not to lock it up" as P. Leroy Beaulieu has said.

There is much truth in the sarcastic remark that the Indian bankers' motive in granting loans is not a laudable one. He trades on the misfortunes of his clients pampering them with fresh loans till they are over head and ears in debt.* The only way to extricate oneself from the money lenders' clutches is to bid farewell to the mortgaged property. The like condemnation cannot be extended to the village banker of the better class, with whose useful services the rural communities of India have at no time been able to dispense. The above description applies to the "marwari" usurer who seems to be the diseased product of a diseased community.

The European banker will not allow his reserve of gold to remain permanently higher than what he considers necessary for the purpose of his business. To do so would amount to neglecting to take a profit in his business which could be safely secured and that is a course which the banker does not adopt. When his reserve is in excess of his requirements the banker lowers the rate of discount, issues credit to a greater extent and sees his reserve gradually reduced

* According to one view "the main cause of indebtedness is the vicious system of credit of the mahajan. All the improvidence, extravagance, the costly marriage feasts or funeral ceremonies and the ruinous litigation are merely due to the fact that the village usurer is too willing to lend for these purposes." *Vide* Indian Co-operative Studies—page 35.

to that amount below which he considers it unsafe to allow it to fall. Owing to the ebb and flow of his business there may be at times a superfluity of gold at the banks or the reserve may fall below the safety limit but the guiding principle is that the supply of gold should be fully utilised. The indigenous banker on the other hand lays much importance on the rate of interest.

Money-changing, i.e., the exchanging of one kind of coin for another. The name "poddar" was given to the banker who specialised in this business. In the former times there was a variety of coins issued from a number of mints.* With the breakdown and gradual disintegration of the Moghul empire the various Indian potentates set up their own mints and minted their own coins. This made the confusion worse confounded. The money-changers used the multifarious currency to their own advantage. The money-changers were the contractors in the native states for the mint. Up till the year 1793 there was an endless source of trouble and disturbance due to the multiform native coinage. The East India Company began to mend matters and not till 1835 could a definite, well-recognised and uniform coinage be issued in silver. Up till this time the money-changers used to ply a lucrative business but now this source of profits has dried up.

* According to Macleod " there were 994 kinds of gold and silver coins of different weights and fineness whose value was constantly varying. Hence attempts to force bimetalism were a failure." —Macleod. " Indian Currency."

Deposits.

The European banker is more a borrower than a lender. He attracts much money in the shape of deposits part of which he utilises in granting loans and overdrafts. Even while discounting bills of exchange the modern banker gives the right to draw money on him and this takes the shape of a book credit with him. The customer can draw a cheque to the full amount or may increase his current account balance with the banker in order to draw on it at a later date. Thus in the civilised communities where banking is fully known and practised, deposits arise in three ways : (*a*) by actual deposit of cash paid across the counter, (*b*) a loan makes a deposit, (*c*) the discounting of a bill of exchange may lead to a deposit. The loan of one bank generally becomes the deposit of another. Thus the banker succeeds in making the community lend so much capital and it is with this borrowed capital he does his business.

The indigenous banker attracts very little money in the shape of deposits. This is partly due to the fact that the "banking habit" has not taken hold of the people as yet. He makes no attempt to attract deposits but he keeps the money that poor people generally entrust to him for safe custody. He pays the current rate of interest which the savings banks or the banks of his locality may pay and there is the moral obligation on the part of the depositor that he should not make a call at any inconvenient time.

There are some indigenous bankers who in the beginning of their career take much care to attract deposits but as soon as they build up a safe and attractive business they no longer care to burden themselves with the onerous duty of attracting deposits and be in a position always to pay them at call. These people consider deposits more a source of hindrance than help to them, so much so, it has been asserted that some of the indigenous bankers have willed down to their successors never to take up the irksome business of attracting deposits.

Again many of the indigenous bankers prefer to receive deposits from friends but not from business men. Full well do they know that money from business people is liable to sudden frequent and untimely calls. So the indigenous banker does not make it a systematic policy on his part to advertise for deposits and attract them by paying a stipulated rate of interest, agreed to at the beginning. Yet it would be quite wrong to assert that he does not make use of "other's money."

To a very great extent he depends for money on his own purse and if he is in need of money he goes to a fellow banker who lends him money at two to six per cent. rate of interest. It is only in the last resort that they go to the Joint Stock Banks for money. Some of them view with hostility the rise and progress of these institutions, but many of them have realised that they are a source of great help to them. Though in one sense they are rivals they confer inestimable advantages to the indigenous banker. They render unnecessary his keeping

a large stock of silver rupees. They facilitate his remittances from place to place. It might pay him to deposit his idle cash and obtain the bankers' deposit rate of interest. They help him much by discounting the hundies. The endorsements of the indigenous bankers make the hundi doubly strong and such a bill of exchange is a perfectly ideal security for the Joint Stock Bank to discount. Thus the starting of more Joint Stock Banks and the extension of their branches in the interior of the country and at the different agricultural centres is a source of direct benefit to him. In many places the indigenous bankers are coming forward to help the starting of new banks and extending branches of old and tried banking institutions.

The Banking Habit.

The absence of the banking habit is not solely due to the indifference and apathy of the indigenous banker towards the deposits of the people. Nor is the want of security in the past the sole cause for the absence of the banking habit. The absence of savings banks or other institutions to store up savings, the frequent occurrence of famines and the poverty of the people must have had also retarded the growth of capital in India. The absence of a well secured paper currency* commanding the confidence of the community was also responsible for

* The issuing of paper currency by the Government of India removed this defect. As the notes became increasingly popular the deposit habit on the part of the people increased to a great extent.

the absence of banking habit. The rise of banking institutions and the tolerable security resulting out of Pax Britannica has given a stimulus to the growth of deposits in our country as shown by the following table.

TABLE * SHOWING THE GROWTH OF DEPOSITS.
(Crores of Rupees.)

Year.	Presidency Banks.	Exchange Banks.	Joint Stock Banks.	Tota
1887	11	4	1	16
1890	18	7	2	27
1897	12	9	6	27
1907	31	19	14	64
1917	75	53	32	161
1919	75	74	61	211
1920	86	75	74	235
1921	72	75	80	227
1922	71	73	65	209

Another curious fact is that the Indian people as a rule never draw cheques on the deposits they give to the indigenous bankers. As Sir R. Temple says, "it is a most extraordinary instance of the mutual distrust between man and man." †

The indigenous bankers that receive deposits now and then can be compared to the London Goldsmiths who have been acknowledged to be the real forerunners of modern banks in England. The London Goldsmiths took care of the money deposited with them and seeing that the whole of the deposits were never called up at once, began to issue notes that passed as money thus building up a machinery of credit that enlarged and extended the usefulness

* *Vide* Statistical tables relating to banks in India 1922 issue.
† *Vide* Journal of the Institute of the Bankers, Vol. I, 1881.

of the actual moneyed capital deposited with them. The indigenous bankers never attempted to pursue such a policy even before the right of note issuing was annexed by the Government in the year 1861.

The Issuing and Discounting of Hundies.

All banking transactions in India are exclusively in the hands of the trading classes especially in the interior of the country. Funds are exchanged from place to place by the well-known device of the hundi. The word "hundi" is a Persian word given to it by the Mohammedans. It is a generic term denoting all instruments of exchange drawn in vernacular. It literally means "to collect." These hundies generally run for an odd number of days that is for 41 days at Benares, Bombay, Mirjapur and Lucknow, 61 days at Fattagar and Farrakabad, 121 days at Lahore and Multan. Some are drawn payable on the 11th and 21st day of issue. Some are drawn as sight bills and these are known as "darsani bills." * The First of the three copies of this bill of exchange is known as "khoka," the second of the three copies of the bill of exchange is known as "penth," the third of the bill of

* Local usages in respect of hundies are so numerous, uncertain and undefined that the Government of India feared to abolish them and the Select Committee of 1878 expressly introduced a saving clause in the Negotiable Instruments Act recognising the full force of local usages. "Dhani" hundies pass from hand to hand like bank notes. The word "dhani" means owner but still it is not interpreted as bearer so as to bring the matter within the penal provisions of the Paper Currency Act. In Shahjog Hundies the word "Shahjog" means a respectable holder of the bazar. Acceptance is not necessary in the case of this Hundi.

exchange is known as "parapenth." The rate of discount is known as "hundiyana" and varies with the state of trade and the standing of the party. There are certain brokers specially the Multanee Bankers of Bombay whose main line of business is to deal in hundies and they obtain handsome profits amounting to lakhs of rupees. The hundi changes hands like the bill of exchange. The dishonouring of a hundi is very rare. The ordinary way of writing a hundi in some parts of the country is by writing transversely across the paper. It bears an impressed stamp and is drawn up in the vernacular "mahajani" as it is usually styled.

Formerly when railway communications were not very much developed, the bankers used to earn much money from this source. But now other means of conveyance of money notably the splitting up of notes into two-parts and sending each part separately, money orders, currency transfers and bank drafts, are being used for remitting money from place to place.*

With the opening of the branches of the Imperial Bank of India a change has come over the situation. Even the Government does not issue a currency transfer on a place where the branch of the

* The "javabi" hundi remits money in this manner. The drawer goes to the indigenous banker and asks to remit money to the payee in another place, whereupon the banker instructs his agents to pay money to the payee. The payee has to attend the office of the banker and give a receipt for the sum received by him. The banker can cancel his order to pay in case the drawer fails to keep his promise to the banker. This partakes more of the nature of a letter of recommendation than a regular bill of exchange.

Imperial Bank exists. They are issued on treasuries where the Imperial Bank has no branch, at the same rates approved for the bank. When postal facilities become interrupted due to strikes on railways or postal employees funds may be remitted by means of these transfers.* But an important part is played by the indigenous banker who finances to a great extent the moving and storing of crops required for local consumption and for export purposes and these loans are repaid to a considerable extent out of money obtained from banks.

The total amount of hundies drawn depends on the amount of internal trade. Mr. G. F. Shirras states that the number of hundies are on the increase but in the interior, specially in Allahabad, Benares and Cawnpore they are becoming fewer due to the fact that there are available at present many cheaper and secure means of remitting money thus dispensing with the use of a hundi.

Again the indigenous banker usually gave drafts upon any place in the world *viz.* Constantinople, upon New York and upon San Fransisco. These letters of credit were drawn after letters of advice were given so that they might be honoured on all occasions.

Discounting Traders' Bills.

The shroff acts as the middleman between the Imperial Bank and the Joint Stock Banks on one

* During May and June 1921 when there was a strike on the Assam-Bengal Railway resort was taken to this method of remitting money.

side and the vast trading community on the other. He buys the traders' bills at a high rate of discount for ready money and when he has not enough money to carry on this business he simply rediscounts these bills at the big banks. The Imperial Bank considers this business safe as the shroff's endorsement makes it doubly strong and as the shroff takes good care as to the nature of these bills there is no danger. Thus he is performing the function of a bill broker of the London Money Market.* Keen competition exists for this kind of business in Bombay and profits arising out of the difference between the two rates of discount is necessarily small. But as in the London Money Market we do not meet with a uniform rate of discount for trade bills in our local markets.

In Bombay there are two sets of the indigenous bankers *viz.*, the Multani bankers and the Marwari bankers. The Multani bankers conduct this discounting business, lend money and confine themselves to banking business proper while the Marwari bankers tansact other business. The Multani bankers purchase the hundies drawn for two or three months and they are discounted generally at 6 to 9 per cent. rate of discount. These are rediscounted at the Imperial bank and the difference between their discount rate and the Imperial Bank rate constitutes the profit for them. The endorsement of

* The only difference consists in the fact that the bill brokers of the London Money Market are chiefly dependent for cash on the banks. " All that the bill broker's capital consists of is a boot and a bill case " but the indigenous bankers are more independent of bank's help.

the native banker is important and necessary and so the trader has to pay this price. Unless a bill of exchange contains two supporters the Imperial bank does not discount it.

There is an association of the Multani Bankers which regulates their rate of discount in accordance with changes in the Imperial Bank rate. There are about 200-250 members and a small committee of 5 members, the most senior of these bankers generally meet and regulate their discount rate. They hold their meetings on every Sunday to discuss common matters pertaining to all of them. The high degree of integrity which exists among this community is a noticeable feature and it is a pity that the Indian Joint Stock Banks do not emulate this noble example.

Other Functions than Banking.

The private banker generally combines business with trade or holds land or does commission business and very often in order to get rich quick he speculates heavily in all kinds of produce. He does mortgaging business which often involves him in litigation. The indigenous banker specially the shroff speculates in Government Paper during the off season but very rarely holds it or lends money on it. Some of the most desperate gamblers in the market of speculation are to be found among the native bankers of Western India.*

* *Vide* Sir R. Temple—Journal of the Institute of Bankers—1881. Sir D. E. Wacha gives a beautiful description of speculation in Bombay during the years 1864-1866 in his book "Bombay Municipal Government" pages 21-22.

At Cawnpore* the native bankers trade in money, cotton, grain, flour and other articles. Some of them manage the sugar works and the flour mills. At Delhi the indigenous banker finances the goldsmiths and skilled workers. The banker of the East adheres to the practices of the guilds that are comparatively neglected by the great money lenders of Europe and counts jewels among his means of trade and not as objects to be kept in his safe. He makes systematic advances to the goldsmiths and sells the finished products himself. He tries to efface the maker of the goods, he sells and poses as the actual producer. Thus he appears to be both a jeweller and a banker. In Bombay the Marwari bankers deal with cotton, seeds, and shares and do much speculation in the value of these things. In villages the rural banker plays a quadruple role. He is the purchaser of rural produce, the local agent of the European mercantile firms, the village shopkeeper and money lender. Thus the general practice is that the indigenous banker rarely does pure banking business alone. Banking, agency, commission, brokerage and middlemen's profits are some of the various avenues for obtaining money.

* There is a bankers' association which undertakes the duty of settling commercial disputes, regulates the discount rate and settles monetary claims. This association is the modern counterpart of what Dr. R. Mukherjee has described as guilds. The Bankers' guilds existed in the past and some specimens of these guilds might still be seen in Jaipur, Multan and Marwar, the original home of these Indigenous bankers.

The Bankers' Associations.

In all the big commercial centres of modern India where a number of these indigenous bankers transact business, they form themselves into an association to protect their mutual interests. Their bond of social co-operation, their sense of economic interest, and the degree of mutual trust is so great that they submit all their commercial disputes to their arbitration courts and their decisions are virtually carried out thus resulting in greater organic and functional solidarity.

Dr. R. Mukherjee says that these bankers' guilds decided not only financial claims but also social quarrels. Sometimes the oldest of these bankers were allowed to arbitrate on commercial quarrels and their voice was taken as final and the disobeyal of their decision would mean nothing short of a social ostracism. The money market would be closed against him. To be readmitted into the fold of the market, the culprit had to perform the well-known prayaschit ceremony and feed a hundred brahmins. He says that "most of the important cities and trade centres have their indigenous banking associations, and panchayats with their particular circles of guild jurisdictions which embrace all the merchants and bankers of the region and the control of such guilds their headmen exercise in the direction of fixing the rates of interest, settling commercial disputes, levying fees in certain transactions and spending the proceeds on humane and religious objects has contributed to a high degree of integrity and mutual interest and

among the classes of people and the development of commercial law in the country on a strictly democratic and ethical basis."

The Native Market Rate.

No separate set of figures has been collected showing how readily and to what extent money flowed from one market to another. Mr. J. M. Keynes says "the native market is ultimately dependent for its funds on the European market." According to him the rates in both markets must move up and down in one and the same manner when money is required during the busy season. The difference between the two market rates is due to the kind of business transactions undertaken by them and to the nature of the security attached to this business. During the last decade of the 19th century there existed no intimate relation between two markets.* Whether these conditions were quite abnormal as suggested by Mr. Keynes or whether the same facts are being repeated every year there is no official means of ascertaining. The wide difference between the two rates would disappear as competition † between them becomes keen

* *Vide* Mr. J. H. Sleigh's letter submitted to the Fowler Commission. This letter explains briefly the nature of the shroffs' work as regards rediscounting of hundies with the Presidency Banks.

† The following table shows how the rates were approximating towards each other in a closer manner than in the past.

Bombay Money Market.

Date		Imperial Bank (Hundi rate) %	Bombay Bazar rate %
April 15	...	7	9½
May 15	...	6	9

and the rates would reflect the nature of different risks undertaken by them. The native shroff rarely discounts foreign bills.* He confines his attention solely to hundies of Indian traders and as he knows full well their commercial standing he undertakes little risks in discounting them. This fact must generally account for the difference between the two rates. The Indian Bank rates are influenced largely by the fact that they have to finance produce for export to foreign markets and for buying raw materials for the Indian industries. Shroff's money finances internal movements of crops and export and money ultimately comes from the banks to repay these advances. Shroff's rate is considerably easy and on account of their financial strength they underquote the bank rate to the extent of one per cent. in the slack season and a great part of the financing of the internal trade is done by him, hence there is no reason why the native discount rate should move in close consonance and ultimately copy either the upward or downward movement of the bank rate but all depends on the stringency of the money market and the demand for money.

Date	Imperial Bank (Hundi rate) %	Bombay Bazar rate %
June 15 ...	5	7
July to November ...	5	7
January ...	8	10
February ...	8½	11¼
March ...	8½	12

Vide Report of the Controller of Currency—1920-1921.

* They take up foreign bills also "if it suits their book" says Mr. W. F. Spalding—in his Eastern Exchange, Currency and Finance.

The Present Position of the Indigenous Banker.

Thanks to the British rule, a well administered government has given perfect security and foreign capital is being invested freely in our country. The growth of banks in this country and the recent rise of the co-operative societies have tended to restrict the field of operation but he holds his own ground in a limited circle. The co-operative banks generally lend for productive purposes and the impecunious man who has to borrow for social functions has been left to his mercy. The rate of interest has been drastically cut short and this is telling very seriously on the rural bankers. The former 25 per cent. has been reduced to 12 or 15 per cent. The urban bankers have been unable to obtain the little deposits that they used to attract before due to the opening of new banks or branches of the existing ones. Their reluctance to finance manufacturing concerns which are rapidly springing up must also go against them. The Individual proprietary basis on which private banking has hitherto been conducted must give place to banks on Joint Stock basis. What India wants is not bankers of this type but banks.

Defects of the Indigenous Bankers.

The indigenous bankers have done very little to manufacture credit. Their bills of exchange *i.e.*, hundies are merely a species of mercantile exchange.* They have never manufactured credit by

* Mention should be made of the 'Jokhmi hundi' which is of the nature of the policy of insurance. This is a peculiar form of marine insurance common to native merchants. There are three parties, the

the issue of notes. They have not financed manufacturers on a large scale.

The essence of banking business consists chiefly in issuing credit and dealing in credit operations as shown by the definitions so profusely quoted at the beginning of this chapter and the indigenous banker has done very little as regards the development of credit beyond issuing letters of credit from one place to another. Deposit holding and the issuing of notes are alike credit operations and the indigenous banker has left both these sources of credit untapped.

Finally one has to observe the lot of direct and indirect services that a bank performs in a modern community. Some of the most direct services performed by the commercial banks are the provision of banking facilities and their extension by a network of branches. Modern Banks are financial service stations. "The Western Banker is a financial focus of the community. He is in constant touch with investors, and can help in selling stocks and bonds. He can advise on market securities, investments, credits and budgets and a thousand

drawer or the shipper of the goods, the hundiwala, *i.e.*, underwriter and the consignee. After shipping the goods to the consignee the shipper draws a hundi and sells it to the insurer for cash which is the value minus the insurance premium charged. The Hundiwala sends the hundi to the agent who on safe arrival of goods goes to the consignee for payment. In case of non-acceptance or non-payment the Hundiwala has to charge the consignor and the consignee. If the ship is lost the Hundiwala has to bear the loss. The only difference between the Jokhmi hundi and the modern Insurance Policy is this—the money is paid to be recovered later when the goods arrive safely according to the Jokhmi hundi.

and one financial questions."* The indigenous banker understands all these but he rarely allows another man to benefit by his knowledge, experience and business acumen. The indirect services are the providing of a sound and stable credit system by enabling the financial machinery of the country to run smoothly. The indigenous banker when weighed according to this standard will be found wanting. With the exception of the hundi business and the issuing of drafts on foreign centres of trade no other transaction of his benefits the community. Of course he is the only thrifty man and the value of his example might be taken as the one other service he is giving to the community.

The indigenous banker is not a scientific banker forbidding gross speculation and refusing to support overtrading or overinvestment. He himself violates all these functions. He fails to perform the elementary duties of a modern banker. As Dunbar has said "to be a bank now at this present day an establishment must carry on the purchase of rights to demand money in the future on securities and it must use in some form or other its own engagements for the payment of money upon demand."

The important role of the Western Banker in aiding production and stimulating the capabilities of the captains of industries by his timely monetary help is not a distinguishing feature of our indigenous

* *Vide* J. W. Mullaly's Article on the "Bankers and the Advertiser". Bankers' Magazine—New York.

banker. The Western Banker does not create credit out of nothing but the control of capital is concentrated at the bank and the banker by means of loans and advances in one form or other enables the persons in whom he has confidence to obtain the temporary use of "others' money." The banker is under the strongest inducement to see that credit passes into the hands of those persons who are able to use it to the best advantage. Other things being equal, credit will pass into the hands of those channels from which its return will be certain. Credit finds its way to those who possess the highest credentials and offer the greatest security for the repayment of advances. The indigenous banker does not shrink from financing industries on industrial securities provided he is satisfied that the business is carried on on sound lines. But on the whole there is no facilitating of the employment of capital on his part. As Bagehot remarks "the Rothschilds are great capitalists but not bankers" one must repeat the dictum that these indigenous bankers are great capitalists but not bankers.

"A nation gets the banking system it deserves" and it is a matter of sincere regret that India of the past rent by internecine warfare and political turmoil could give no free scope to the growth and development of real, and legitimate banking business just as the Western countries have developed.

The efficiency of a banking system should be tested by three crucial tests namely stability, adaptability, and initiative. By stability is meant firmness

and security from all outside dangers. When credit is rudely shaken the banking system should possess not only inherent strength but capacity to restore public confidence. This quality is the *sine quâ non* of all panking business. By adaptability is understood the power to adjust itself to new conditions and when trade and industry are making progressive strides the banking system should be able to extend its scope of business and undertake new functions to suit the changed conditions of social and industrial life. By initiative is meant the quality of creating new developments.

The indigenous banking system possesses to a remarkable degree the quality of stability. The conservative lines on which the business is conducted, and close business knowledge of the several customers and the cautious way in which loans are granted conduce to stability and so long as the indigenous banker pursues the principles laid down by his ancestors there is no danger to him. But the indigenous banking system is woefully wanting in adaptability and initiative.

Suggestions for Improving their System.

Modern economic development is so rapid that to-day's aims and methods become antiquated very soon and the indigenous banking system which is still conducted on time-honoured and stereotyped lines has not so far displayed any signs of adaptability. It has been the cry in India ever since industries began to be organised on Joint Stock

principle of management, that more capital should be accumulated. Thus it became clear that the first duty of the indigenous banking system should have been to mobilise the money power of the country and provide the needed credit for the industries to run in perfect order.

But the indigenous bankers have never devised any scientific means to stimulate thrift and encourage the saving habit on the part of the people by systematically attracting their deposits. Secondly they have not acted as the middlemen between the savers of capital and the entrepreneurs who have needed the capital. Theirs is purely a selfish and sordid motive, namely that of interest. So long as a high rate of interest can be procured, the indigenous banker will lend money for unproductive purposes even. In Western countries, " Banking accommodation stimulates production and increases consumption." In the case of the indigenous banker the loans are sometimes granted for unproductive purposes and the result is destruction of capital and sheer economic waste. He should realise that a bank is a reservoir of liquid capital which can be directed here and there when it is needed for temporary or seasonal use and thence be returned to the reservoir for another mission. Credit is not an end but a means to an end and hence it is necessary to ensure that money is advanced for a useful purpose.

Up till now no signs are visible that the indigenous bankers are going to call for deposits. This they decline to do because it involves risks and

a crisis may ensue if they mismanage the funds allotted to them or lock them up in unrealisable assets. But it is high time that they should bestir themselves and do their best in promoting the newborn industrial activity spreading over the country. The people know these bankers intimately and will be willing to entrust them with their savings. The machinery of the Joint Stock Banks as regards the deposits is cumbrous and little understood by the people. So they will certainly prefer the indigenous banker so familiar to them to the Joint Stock Banks which have to be managed by outsiders or foreigners. In case there exists no co-operative bank in a village the next best thing is to induce the village mahajan to take up this policy of attracting deposits and pay for them. No doubt this is irksome to him but such a progressive policy will ensure the success of many industries and obtain much reputation for him for facilitating our onward industrial march. Next to the co-operative banks, he will be the most successful agent that can succeed in gradually weaning the people from their hoarding habit or converting their savings into ornaments.

The indigenous banker is lacking in initiative. He has not taken the lead in new lines f develapment nor has he opened any fresh avenues of expansion. The successful development of our cottage industries can be easily taken up by these monied people. The village mahajan finances the agriculturist and granted that there is a favourable monsoon and profitable employment of capital the

mahajan obtains the capital lent and during the non-agricultural seasons it has to lie idle in his hands as there is no demand for it.* This money can profitably be utilised in encouraging local industrial talent and as the mahajan knows fully the success or otherwise of such an attempt on his part he ought to make that attempt. Such legitimate promotion of cottage industries on his part but not sweating and exploiting as is the case now would not only earn him a fair return of interest on his capital all round the year but it will enable the struggling agriculturist in many instances to eke out their own livelihood and increase their famine-resisting capacity.

The indigenous bankers have never attempted to standardise the form of the hundies. There is a bewildering variety of usages as to their form, execution, endorsement, negotiation, discounting, and payment.† A unification of these different systems would be of much benefit to inland trade. This is the task that should be undertaken by the indigenous banking associations. Although the bulk of the hundies is of the usual English style that is used in the foreign trade of India, yet a complete uniformity is necessary in the case of these bills used for inland trade.

The indigenous banker has not realised the higher duty of a bank. The primary duty of it is to

* The mahajan must try to make them capitalist producers but not his own serfs as it has been the case, in agriculture. He should have an interest in the economic welfare of his clients.

† An idea of the different variations in the local usages in the matter of hundies can be obtained by consulting the "Indian Negotiable Instruments Act," by K. Bhashyam and Adiga—(1917 Edition).

earn dividends for the shareholders. The next higher duty is to help the trade and industry of the country, to stabilise the financial machinery and provide stable credit for the millions of its inhabitants. The indigenous banker is not fired with the necessary zeal and enthusiasm to realise this high ideal. He seems to be careful of his own materialistic aims and pursuits. Many of these indigenous bankers are hidebound by caste or conservatism. They lack driving power. They have prudence, business judgment and sense of relative proportion. They need aggressive constructiveness, enthusiasm and above all imagination and without these there would be no progress.

Whatever might be their shortcomings and whatever their faults have been and are it must not be denied that they are rendering signal service to agriculture and internal trade. It behoves them to set aright and adjust their system to the new and altered condition of our industrial life. They should realise the higher aims and loftier ideals of a banking system and act up to them so that they may deserve fully the appellation of "bankers" which is now applied rather indiscriminately to all the big capitalists and money-lenders of our country.

Other Quasi-Banking Institutions.

The indigenous class of institutions, *viz.*, the "kuthe-chitte" and the "nidhis" of Madras have been performing money-lending business from a long time since. In the Kutthe-chette system a

number of men unite to put some specified sums in some specified time and the whole sum is drawn in a lot and the winning lot takes the whole sum. Next month a similar lot is drawn and the previous winner is excluded. Thus this process is continued till all the subscribers have received their lots once. The sum is repaid in easily payable monthly instalments. The "nidhis" originated in the year 1850. The etymological meaning of the word "nidhi" is treasure. These are associations for mutual credit. The main object with which they were started was to facilitate savings, relieve members from old debts, and grant loans for all purposes on good security. Outsiders were also given loans at a higher rate of interest. Now there are two kinds of "nidhis," the permanent and temporary.* Although these societies started at about the same time as the co-operative societies in Germany they had no such brilliant career as the latter. This is partly due to the fact that frauds were committed at the early stages of their existence and want of supervision must have had its effect. The method of monthly instalments and the paying of them in clock-like regularity requires some education and thrift on the part of the shareholders and the nidhi system consequently proved unsuitable to the agricultural population. In spite of these defects these nidhis are still flourishing says the banking blue book but no statistics of their number, capital and shareholders have been collected.

* *Vide* Statistical tables relating to banks in India 1917 publication.

Sir Frederick Nicholson has pointed out the good features of the nidhi system thus—" They are the introduction of co-operative principles and habits, the stimulation of thrift and providence, the inculcation of business habits and punctuality, the cheapening of credit, the insuring so long as rules are observed that the members will if non-borrowers get back their money with interest and if borrowers they are secured from all annoyance so long as they pay their dues punctually, business is extended by cheapening loans and not entrapping the unwary and ignorant, profits are to be sought by the development of cheap credit and not by squeezing the individual debtor—small savings are cared for and petty capital retained in the neighbourhood." *

The nidhi system is a good institution for encouraging thrift but so long as they are managed well they work well but owing to growth or indifference the management may fall into bad hands. The system has been perfected more or less and is not capable of any further extension. Besides these are mere money-lending societies lacking the fundamental conception of a banking institution. " There is no concentration of idle hoards for productive purposes " as Sir Frederick Nicholson puts it. The co-operative credit societies fulfil their duties more admirably and there should be an extension of these institutions. The nidhis have already fallen to the background.

* Sir F. Nicholson " Report on Agricultural Banks " Madras Loan Societies.

CHAPTER VI.

INDUSTRIAL BANKS.

Need for Finance.

That industries need finance is a self-evident proposition. Either to increase production or to buy more raw materials or to extend the site of the factory or to increase the wages of the labourers, capital will be required. The entrepreneur needs capital on the strength of the industrial securities he possesses which are generally as follows: (1) The land on which the factory is constructed if it is the property of the industrial concern. (2) The factory building in which the business of manufacturing is carried on. (3) The implements, tools and machinery which are required for aiding the manual labourers in the process of manufacturing. (4) The portion of circulating capital which is set aside for the payment of wages of labourers and the clerical staff of the factory and some contingency funds laid down for the future use. (5) The raw materials that have been purchased with a view of being turned into finished products. These are the properties at the disposal of the entrepreneurs, and on the strength of these securities capital should be obtained for any of the abovementioned needs.

The Inability of Commercial Banks.

But the ordinary banks or "Commercial Banks" as they are styled are not in a position to

grant accommodation for the following reasons.—Firstly, a banker is not an expert in the matter of land and building valuation; the value of the land might deteriorate on account of social conditions and it may land him into a course of protracted litigation if the rights were not to be securely guarded and the ordinary banker does not care to scrutinise all these carefully and grant the needed accommodation. In fact neither has he the inclination nor the time required to value carefully these securities. Again buildings and machinery would fall in value if the company were to cease production for a time. The Machinery unless looked after will be valued as old iron and nothing more. The raw materials the entrepreneurs might be of such a nature the value of which the banker might not easily estimate and so it is not possible for the entrepreneur to persuade the commercial banker to give the needed accommodation. The possibility of a labour strike, the perishable nature of the article mentioned and the possibility of foreign competition will have to be considered. As the enterpreneur is not in a position to satisfy the commercial banker as to the nature of securities he has to offer the commercial banker refuses to grant the exact amount of capital which the industrial securities warrant the enterpreneur to demand. The securities that satisfy the dictates of prudent commercial banking should possess the following features.

As George Rae says "they should be well-known and be of a definite nature. They should be readily convertible into cash. The pledger's title

should be unquestionable. They should be legally pledged to the bank. They should secure a specific debt. They should be accurately described. They should be of sufficient value, to cover the indebtedness, possibly expenses of collection and contingent charges. They should be definitely located. The pledger's character should be prudent and industrious. The securities should be of such a nature as to possess stable value. A perfect banking security should combine ultimate safety, a certainty of payment on a specified and not a distant day, a capability of being converted into money in cases of unexpected emergency and a freedom from liability of depreciation." * The industrial securities do not possess these characteristics. Besides this reason, the commercial banker thinks that the investment of short-dated deposits in non-convertible securities is hardly consonant with the sound canons of commercial banking. Any bank that unites the three lines of financing agriculture, industry, and commerce in its hands is sure to come to grief.†

Specialisation.

On the European continent, the state filled up the gap between commercial banks and industrial companies by starting discount houses for temporary periods and when this necessity was no longer felt they had been withdrawn.

* *Vide* George Rae—Country Banker.

† The Punjab Bank failures are an evidence of the glaring violation of this acknowledged principle.

But now special banking institutions exist for these three purposes. In France the Credit Agricole takes up agricultural finance into its hands, the Credit Foncier takes up the business of mortgage loans and loans to communes and thus provides long term credit. The Banque de' Paris et Des Pays-Bas takes up the financing of such industries as railway building, harbours, tramways, electrical enterprises and frequently acts as the manager of syndicates for promoting industrial concerns.

In Germany the Raiffeisin Co-operative credit societies and the Landschaften take up the business of agricultural finance. The small producer and the artisan is looked after by the Schulze Delitzch type of co-operative societies. The Preussiche prand-brief Bank and Preussiche Central Bodencredit look after the mortgage business. In addition to these the Gross Banken play an important part in the financing of industries.*

* The German Gross Banken perform the following banking operations : (1) attracting deposits (2) giving loans (3) discounting bills (4) capitalising industries (5) floating new industrial companies (6) regulating the value of the shares by buying and selling (7) buying and selling securities largely on their own account. All banks are members on the Stock Exchange. As Dr. Reisser explains—these were forced to take up all these ultra-commercial operations in order " to meet the real demand of German economic development." Although they adopted a helpful attitude towards German Industries they were managed very well from the beginning. They had a high paid-up capital of their own and attracted long term deposits. They always " combined " to help the financing of large industries. The Deutsche Bank acquired interests in the smaller banks and thoroughly controlled their policy. The policy of the German Banks interlocking themselves with industrial companies led to their development. As Leopold Joseph says the German people have full confidence in the

In Japan the Yokohama Specie Bank has been established to look after the mechanism of foreign exchange and attend to other commercial purposes. The Hypothec Bank of Japan modelled on the Credit Foncier looks after the agricultural interests. The industrial bank is based on the model of the Credit Mobilier and is a financial organ for helping industries.

In England the British Trade Co-operation was recently established to grant larger and longer credits than the existing banks for the helping of the British producers. Thus everywhere there is a line of distinction drawn between the financing of agriculture, commerce and industry.

The Need for Specialisation.

It is a well-known fact that the nature of capital varies in the three lines. "In commerce the money invested is brought back immediately by the disposal of the merchandise and so a long credit is not needed. In Industry the capital becomes fixed in raw materials and is restored as soon as the raw materials are manufactured and sold. The capital invested on agriculture returns slowly by annual instalments. Regarding the certainty of

administration of banks and in the integrity of boards of directors which are mostly composed of capable men. Stringent regulations are in force and it is only a serious catastrophe that can shake their confidence. If our banks wish to imitate their tactics it is absolutely essential that they should employ the same precautionary measures as the German Banks.

redemption the capital invested in commerce is influenced only by artificial market fluctuations while agricultural pursuits are affected by natural causes uncontrollable by human energies, so that, to this extent, the return of capital in agriculture is uncertain. As regards the renewal of capital agricultural pursuits unlike the other two lines, require little, the period for which the capital becomes fixed being long, unless the land purchased meets with some catastrophe. In industry an early renewal is necessary to a certain extent owing to wear and tear of plant and buildings and to the sale of the articles of manufacture. In commerce the term of fixed capital is shortest, renewal being necessitated on the sale of the goods." * Thus the operations of capital are bound to vary in the three pursuits and so there should be three kinds of Capital.

The Present Situation in India.

India is a slow starter and she has now started in right earnest on the long road leading to industrial development and to help her on this long and costly journey capital is needed. By adopting a policy of "discriminating protection" the Government have not only indicated "a change of heart" but have proved that they are bent on

* Quoted from the article on the Japanese Banking system—American National Monetary Commission.

placing India's industrial equipment on a par with that of the rest of the world. Political feelings are leading to a combined campaign of boycott of foreign goods and the encouragement of "swadeshi" goods. It is keenly felt that India must employ its own capital and that capital should be handled by Indians or she should develop her manufactures with foreign capital under Indian management. It is also an accepted fact that India need not necessarily copy the Western industrial organisation on a wholesale manner, thus intensifying the existing evils of overcrowding in cities and the slum areas round factories. Small-scale organisation of the cottage industries with proper facilities for the training of the artisans, for the obtaining of the latest information, for the provision of capital and adoption of businesslike methods is no less important than the adoption of the factory system of large-scale production. To accomplish any of these objects more capital is needed.

Recent experience in connection with Government and of company flotations has proved that capital would be forthcoming in India if only the needed facilities for mobilising capital are furnished. It is not only ordinary banks conducting commercial financing that are needed but industrial banks are necessary to help the current enterprises of our country and help the starting of industrial concerns by underwriting the shares of newly started concerns.

The Imperial Bank is prohibited to do this business by its bank charter. The other banks slavishly model themselves on these lines hence the

financing of industries is in a backward condition.* No doubt the co-operative credit societies are doing something to alleviate the hard lot of the small producer and the artisan. But the middlemen sellers of the articles are strong and the co-operative societies are not the sole remedy. The village-mahajan finances them but his rate of interest is prohibitive. He does not possess the patience and disinterestedness which are absolutely necessary in the matter of financing industries. His predatory profit seeking instincts make him a hard task master. He generally finances the cottage industries on the advance system by which funds are given in the shape of raw material or cash and this loan has to be repaid by the sale of manufactured goods at specially low rates. The rates of interest generally works out at twenty-five to fifty per cent. and the practical result is that the artisans are little better than slaves. "The artisans cannot even change their employers as a civil suit and arrest were held over them *in terrorem*." † The foreign capitalists wish to have all the loaves and fishes to themselves. If national development is to be on a

* The existing banks cannot lock up their money in long term loans to industries. After the crisis of 1913-15, deposits generally are made for short periods, *viz.*, four months or so. They charge unusually high rates even for short-dated loans to individual concerns. They take a very wide margin in their favour *viz.*, 20 to 25 per cent., and this is a great handicap to industrialists. So Indian-managed Joint Stock Banks for the purpose of industrial financing should be started. They should rely in their capital or upon deposits attracted for six or seven years.

† *Vide* The evidence of Mr. A. E. English—Registrar of Co-operative Credit Societies—Burma—Indian Industrial Commission.

really encouraging scale this unscientific method of industrial financing should be remedied as early as possible by the starting of industrial banks.

The Duty of Industrial Banks.

More industrial banks which are in touch with the small industrialists and which are fairly able to estimate well the prospects of a large range of industries and which possess sufficient money which can be locked up for a long time are an important desideratum for promoting the new-born industrial activity of our country. These industrial banks should possess a large amount of paid-up capital and attract deposits payable after a number of years. If additional capital is required it should be raised by means of debentures which may be repaid after a period of 20 or 30 years. The amount of capital that can be raised by this means can be locked up with impunity. The industrial banks should have nothing to do with short term deposits, remittance of money and the other ordinary commercial banking business. The Indian Industrial Commission has recommended that these industrial banks should take up ordinary banking business. This is no doubt due to the desire to mage these concerns profit-paying ones and whether such a thing should continue in the future will mainly depend on the number of industries forthcoming for help. If demand for industrial finance is keen, it would be unwise for these banks to conduct a mixed business.

Thereby they would be defeating the very object and intention with which they have been started.

The industrial bank should not finance solely one single interest or a single group of interdependent interests because the bank's fate will be identified more or less with the industry and will be ruined in case any calamity befalls that industry. Hence it is unwise to identify the interests of the bank with that of one industry. The way to help new industries is to supply initial capital after carefully examining proposals or provide money loan after the industrial concern is floated in the market. It can grant loans on the industrial securities of the concerns or it can underwrite some of the company's shares itself. But it is essential in this case that the Directors of the bank should first of all know something about the undertaking. It should be wise if it were to employ specialists in those business lines to examine the proposal and pronounce their opinion on the further prospects of the individual undertaking and be guided according to their advice. It should wisely distribute its capital, *i.e.*, loans on plant, buildings and lands should be well considered and limited in each case but it is always in its interests not to invest a large proportion of its capital in providing working capital to new concerns. The success or otherwise of the bank would depend on the limitation of each class of business to its proper proportions. But of course when it supplies much initial capital, it should take care to protect its own interests by employing one or two of its men as directors of the new concerns.

The task of rendering financial help to all industrial concerns lies before the industrial banks that have arisen and that are yet to arise. They should be able to give expert advice and encourage qualified Indians to take up the manufacturing lines where there are possibilities of success. Each Industrial bank should publish circulars stating the few industries that can be taken up successfully and promise to accommodate all pioneer manufacturers with the necessary finance.

The Existing Industrial Banks.

The first bank to undertake this new type of banking business was the Tata Industrial Bank. Modelled on it several other banks have been lately started and they profess industrial financing as their avowed mission.* Many of these wish to

* The Tata Industrial Bank was the pioneer in this direction. To-day we have the following industrial banks doing business in British India :—

Name of the Bank.	When registered.	Place of business.
The Tata Industrial Bank ...	11-12-1917	Bombay and 11 branches.
The Industrial Bank of Western India.	1-10-1919	Bombay Presy.
The Surat Industrial Bank ..	30-3-1920	Ditto.
The Karnani Industrial Bank ..	20-9-1919	Bengal Presy.
The Indian Industrial Bank ..	26-10-1919	Ditto.
The Raikut Industrial Bank ..	2-1-1920	Ditto.
The Sthal Industrial Bank ..	23-12-1919	Ditto.
The Monghyr Industrial Bank...	23-3-1920	Bihar.
The Simla Banking and Industrial Co.	1-10-1919	Delhi.
The Assam Industrial Bank ...	17-5-1919	Assam.

imitate the German Gross-Banken in attempting a similar kind of business. But they are totally lacking in initiative and promoting vigour which is a characteristic feature of the German Banks nor have they the requisite capital and knowledge. They are little better than mere machineries for raising capital and much cannot be expected by their unco-ordinated action. Industries cannot be successfully worked as small independent units. Hearty co-operation should exist between the industrial, commercial and financial communities. As Sir T. Holland says "industries cannot flourish singly but in family groups, provinces do not develop singly but in federal associations. For the essential communications for necessary raw materials, for markets and for financial aid and even for unskilled labour one province must rely on the resources of another."* As the Bombay Industries Advisory Committee states " The establishment of a central industrial bank or similar organisation with a large capital and numerous branches designed to afford financial support to industries for longer periods and on less restricted security that is within

Even in the native states industrial banks have been started with the sole desire of fostering industries.

Name of the Bank.	When registered.	Place of business.
The Mysore Industrial Bank ...	24-6-1920	Mysore.
The Gundulpet Industrial Bank	24-7-1920	Do.
The Central Travancore Industrial Bank.	13-9-1919	Travancore.
The South Malabar Industrial Bank.	6-4-1920	Cochin.

* *Vide* Journal of the Indian Industries and Labour—Feb., 1921.

the power of practice of the existing banks is urgently needed as in the case of Japan, a certain amount of Government aid and Government control are also necessary for its safe working."

The delegation of industries to provincial control, the appointing of a popular minister, in touch with the needs and aspirations of the Indian Industrialists, as head of the Industries Department, the formation of Industrial Boards in the various provinces to help and guide the deliberations of the Industries Department are useful steps in the right direction but the starving of the transferred departments is too well-known.* Without adequate funds even for the undertaking of scientific research in the several industries very little can be accomplished by the state in the direction of industrial development.

Suggestions.

In Great Britain the British Trade Corporation undertakes to organise study and research into

* It must be admitted that the Meston Award is primarily responsible for this. The industrial provinces like Bengal, Bombay and the United Provinces have very little left to them, to be utilised for the nation-building departments. More resources should be granted to them so that they may discharge their duties properly and aid the development of national welfare. Only direct taxation is left to the Provincial governments. Indirect taxation lies solely in the hands of the Central Government and it has also two of the most important direct taxes namely Income Tax and Super Tax in its hands.

The Central Government should not encroach further upon the field of direct taxation. Again the transferred subjects should be given more money as soon as promising schemes of development are designed by the ministers.

new ideas and inventions and examine and nurse new schemes or development until sufficiently proved and ripe for public investment. The Corporation tries to act as a "link between the British investor and British industry." Our Industrial Banks should have this lofty ideal before them rather than be mindful of their own interest and attend to ordinary banking business also. There is no use of merely granting loans on approved securities to the existing industries. They must float undoubted industrial companies underwriting their capital and offering the public ample facilities to invest their humble savings in these new undertakings so that they should not only be helping the existing industries but actually create new industries where there are possibilities of success. If Indians possessing the necessary individual initiative and resourcefulness are not to be had, they should persuade enterprising entrepreneurs of the West to go over here and take the raw materials into manufactured products rather than allow them to be shipped to foreign countries only to be re-exported to India as finished products. This process will enable the Indian industrialists to gather first-hand technical-knowledge and adequate experience from the foreign manufacturers' hands. Then only can a great impulse be given to industrialism in our country.

Again the industrial banks must realise that the Indian investors have no proper guide at present to guide their savings into productive channels. They

lock up their savings in the post office savings banks or employ them in unremunerative forms of employment. Such misdirection of savings and their wrong use should be checked, and the industrial banks should stimulate the promotion of new industrial undertakings and carry them to a successful conclusion. India is capable of becoming industrially one of the prosperous countries if only the industrial banks can supply the needed enterprise and provide effective finance and induce for some time to come the required technical experts to come out from the West and settle here. Our own capital is inadequate and our business knowledge, technical skill and banking experience are limited and till there is a marked improvement in these lines co-operation with British capital, British enterprise and British business knowledge is absolutely necessary. Our industrial banks should work in close harmony with the existing foreign capital in our country and try to create the investment habit in the minds of the people.

The next great want of our industries is widely directed State help. What Government can do for industries is amply illustrated in the case of Japan and Germany. The Government of India professes sympathy and lays down as its policy the successful promotion of Indian industries. The Government of India besides lending practical help to industries, should stop foreign exploiters from placing any difficulties in the path of our industry. It should put an end to the differential treatment of European and Indian industries by the Railway

Companies.* India need not go through the long apprenticeship of patient trial, research and experiment by which the industries of the European countries have been built up. By engrafting on her economic system some of the features of industrialised Europe she can earn an "unearned increment." An industrialised India will be a tower of strength to the British Empire.

* The Railway Board has no doubt issued a circular on May 18th 1915, to the Railway Companies pointing out that the Development of Industries would increase their business and that the Railway Administration should do much for the encouragement of industries by the quotation of favourable rates for the carriage of raw materials and of finished products. They were also asked to co-operate in making a special endeavour to do all that was possible for the encouragement of the Indian industries. But these excellent intentions of the Government get whittled down to precious little while filtering through the administrative strata of the Railway Companies. Before the three Committees of 1918, 1921 and 1922, namely, the Industrial Commission, the Railway Committee and the Fiscal Commission several of the witnesses spoke disparagingly of the Railway rates policy. The proposed rates tribunal would give a fair judgment as between the trade and the railways and would arrange the railway rates on a sounder foundation.

CHAPTER VII

MORTGAGE BANKS.

The 20th century is a century of specialisation and the tendency towards specialisation is visible in banking business as in all other walks of our business life. The English banking system exhibits the specialising tendency to a very marked degree. The ordinary commercial banks or "cheque-paying banks" take up the business of attracting deposits and distribute their capital in loans, over drafts and discounts.* They make every effort to meet the short-term credit requirements of commerce, agriculture † or industry. The "discount" business is specialised by bill brokers and the big discount houses which run a much bigger book than the individual or "running" brokers. The "acceptance" business is looked after by certain merchant

* Vide Hartly Withers, Meaning of Money.

† "It is often stated in the United Kingdom that the commercial banks do not treat agriculture sympathetically as they do the Urban interests. The disappearance of the old country banks and the extension of branches of big joint-stock banks whose policy is guided by the London Board, and the draining away of the rural deposits to Urban areas for commercial and speculative purposes at home and abroad are considered as leading to the unsympathetic treatment of the agricultural interests. The banks refute these charges of unsympathetic policy, unfamiliar managers and discrimination in favour of commercial investment and point out that more agricultural loans are outstanding to-day than in the case of small local and private banks. They point out that there is keen competition among the joint stock banks to develop their agricultural connection. Overdrafts, unspecified as regards purpose are frequently granted in preference to loan accounts.

houses though to a certain extent the commercial banks are becoming the watchdogs over the volume of acceptance. The British Trade Corporation was started in order to grant longer credits to industries and trade and any competition with the existing commercial banks is altogether eschewed by certain rules in its charter.* Specialisation has extended so far that certain kinds of customers have developed the habit of conducting their business exclusively with one bank alone.†

The same specialising tendency is visible in the Japanese banking system. There are five distinct kinds of banks which deal with home trade, foreign trade, industrial business, agricultural business, and colonisation business. Besides these there are a large number of co-operative credit societies transacting business.

It is only in the country of Germany that the Grossbanken perform a mixed kind of business.

The old bank managers are still in office and local directors are recruited to help the new managers in the matter of studying local characteristics of business. Both in England and Scotland the banks have largely invested in loaning to agriculturists to meet their short-term needs. The sureties are conjointly and severally liable and are bound to the extent of the principle plus three years' interest. The rate of interest charged appears to be five per cent." *Vide* report of the Chambers Committee on agricultural credit.

* Besides these there are other schemes of industrial and mercantile banks in London with regional banks for trade and industry and international credit and discounting institutions.

† An account with the Bank of England is considered as a commercial " coat of arms." Coutts and Company was considered as the bank of the fashionable society. (It has recently been amalgamated with the national provincial and union bank) Cox and Company was regarded as the Military Bankers (now amalgamated with the Lloyds Bank).

These German credit Banks * are as Lord Inchcape styles "The clearing banks, acceptance houses, issuing houses, discounting company, promoting Syndicates exchange brokers, traders, and bankers." Doctor Reisser has taken much pains to show that this has been due to historical conditions and that these credit banks are called upon to help the process of industrialisation.

In India, although the system of banking conducted on western lines is still in its infancy it exhibits some signs of specialisation. The Imperial Bank and the Indian joint stock banks finance the internal trade, the exchange banks deal with foreign trade and its finance. The co-operative societies and the post office savings banks try to encourage thrift among the poorer classes. A few industrial banks have arisen recently to finance industries but they are doing ordinary banking business. They unite deposit banking with different other operations. The task of keeping assets of a sufficiently liquid character in order to balance the demand obligations of a commercial bank is no slight one specially when operations partaking of a permanent character such as industrial finance are attempted. Many an authority † has

* As the Economists put it "the German banks are stock, bill and exchange dealers and brokers, banker merchants, trust, financial and promoting companies"—the Economist, October 21st, 1911.

† W. R. Scott says "there is an over-expansion of credit caused by the exchange of investment securities for checking accounts and that a forced liquidation of these securities to meet the depositors' call entails a great loss and an enforced liquidation may bring about a commercial crisis."

written deprecatingly of this tendency and points out that it only paves the way to commercial crisis.

Instead of combining such risky operations in the hands of a single bank, however pressing the necessity of a liberal financial assistance to our industries and agriculture might be, it would be better business if banks were to specialise in long-term loaning. If separate financial agencies are created our banks need not like the German banks be nicknamed " Alerlei enterprisen " and maids of all work or a kind of financial Universal providers. However much our banks may be animated with a desire to emulate the bold daring yet fruitful policy of the German banks they should realise that the small amount of their paid up capital, the low proportion of their cash reserves and liquid assets, the short term nature of their deposits and the absence of masterly financiers are real limitations warning them of the dangers involved in their ambitious programme to obtain absolute control over foreign trade, commerce and industries of our country.

The long-term credit requirements of industri and agriculture have not been studied carefully. The mortgage banks of the joint stock type or co-operative mortgage associations do not exist in this

H. M. Gaiger says " that the practice of commercial banks to invest their sums has been one of the causes of industrial failures in the U. S. A. of several enterprising men who have seen their plane shrivel up and disappear under the sheriff's hammer to satisfy a note that had been called.

C. A. Conant in his modern banks of issue points out that the Bank of Italy, tht Bank of Naples, the Bank of Sicily and the Roman Bank locked up in investment all their notes and failed miserably in 1892.

country. Sir James Meston divided the banking system into four departments. There is first general banking, secondly, the land mortgage bank, thirdly, the co-operative bank and fourthly, the industrial bank. Specimens of the first, third, and fourth kinds exist in our country. But the second one namely, the land mortgage bank has yet to be created. Mortgage banks are included under the heading of Indian joint stock banks and some of them like the Allahabad Bank, Ltd., lend on equitable mortgage but there is not much of specialisation of this business done by them.

The chief reason why mortgage banks should be started is the fact that in the interior this business lies in the hands of the indigenous banker and members of the wealthy class. Their terms are too high and exacting. The borrower is exploited according to the urgency of his needs and nowhere does he get fair terms to which he is entitled by virtue of his security. Organised credit should be substituted in place of the money-lender. As Sir Frederick Nicholson has said " the individual system of providing credit is too elementary and need must make way to higher and more organised form of credit as general wealth, order, business confidence and habits of association develop on the part of the people." These alone can eliminate the dangers of usury. No amount of tinkering with laws can stop it.

The model on which such mortgage banks should be built is that of the Credit Foncier and the European mortgage banks modelled on it. In

Germany the Hypotheken Banken meet the needs of long-term credit on urban real estate. They were established during the years 1862-1872 and many more arose during the great building boom of 1894 to 1896. Most of these banks minister exclusively to the demand for estate credit and some others combine this speciality with other lines of banking.

The object of such banks should be the redemption of ancient and oppressive private mortgages by granting long loans at moderate rates of interest. When a number of such institutions transact business the present abnormal rate of interest will be reduced and it will break the monopoly of the usurers. Their business is to grant mortgage credit without requiring any declaring of the object or purpose of the loan. These should resemble the small Joint Stock Banks of Switzerland. A big mortgage bank situated in a town may find enough employment for capital and it may not condescend to transact business in rural parts. Urgent help is needed in rural parts also and city capital should necessarily be shifted to these parts. The union of town economic forces with those of villages is absolutely necessary.

Mortgage cannot be considered as the road leading to ruin. This is not true in every case. Sometimes it may happen that a man's capital might be locked up in land, houses, stock, eac., and suppose it has to be temporarily mobilised for an occasion. In such a case raising credit by mortgaging the property is not to be objected to, nor is borrowing at such a time by mortgaging a sign of

weakness. But if the borrowing is not temporary mobilising of capital but chiefly due to improvidence and recklessness it is to be condemned as necessarily leading to ruin. But so long as a fair and equitable proportion is maintained between the liability and the assets and the rate of interest is not too high to be covered by the return on borrowed money, mortgage builds a fortune for the borrower and there is no reason to repent for the transaction.

The Mortgage banks should be welcomed for their competing capacity with the money-lender. As Sir F. Nicholson has said " Competition is the only way of bridling the money-lender." * He must be of no account in general credit. The competition of these banks would knock down the present high rates of interest.

It is not the urban borrowers alone that are the chief sufferers on account of the absence of the mortgage banks. Credit is needed for the agriculturists and it is an essential element in the productive process. Fundamentally credit plays the same part in agriculture as in other industries. Credit for the agriculturists should be so designed that it is able to meet short-term as well as long-term demands. Agriculturists require short-term credit to meet

* Sir Daniel Hamilton says " the interest rates of 30-60% due to the indigenous banker must be lowered. He is so emphatic in the condemnation of the indigenous banker that he says ' what India wants is an act written not with a goose quill dipped in milk and water but with an iron pen dipped in the blood of the mahajan, for until the banking system for which the mahajan is dead, India will not live."—*Vide* Souls of Good Quality and other papers.

current outgoings, to facilitate the production and the marketing of their products. They require long-term credit to make permanent improvements in land and extinguish the present amount of indebtedness by lifting mortgages on it.

It is imperative to examine the means available for the agriculturist to obtain credit, either for enabling them to continue agricultural operations or to enable the agriculturist to effect various improvements in his land to adopt machinery and modern scientific methods of farming, to build up a financial reserve against low market prices and to allow his land to lie fallow, to raise better breed of cattle, to experiment with other than the cheapest manures, and to insure his cattle.

The present system of financing the agricultural industry either for short-term or long-term needs is partly good, partly indifferent and very inadequate. The existing financial agencies are the village mahajan or the co-operative banks or the government directly granting loans. Coming to the money-lending methods of the village mahajan enough has been written already in the chapter on the indigenous banker. As an agricultural banker he is a total failure. He is not interested in agriculture, and measures for agricultural progress do not appeal to him. He does not insist on repayment in small sums. He is generally unsympathet the sad plight of the agriculturist. His rates are usually high. Hence a more sympathetic lender of credit is essential.

The encouragement of the co-operative societies has produced very good results. It is an indisputable fact that they form a substantial contribution to the solution of short-term credit requirements of the agriculturist. The fascinating growth and real progress of the movement cannot be doubted by the most sceptical of its critics. But the ideal temperament and requisite character required for its success are not to be found in all men. The government should not rest satisfied with this single form of activity but should supplement it with other means so as to develop the agricultural resources of the country in a shorter time if possible.

In addition to the indirect method of financing agriculture by facilitating the co-operative movement the government has tried to finance agriculture by direct methods. By the Act No. 12 of 1884, known as the Agriculturists Loan Act, the government has undertaken the duty of providing for the relief of agricultural distress. This Act has failed in its duty, for very few individuals alone can be benefited. To secure these loans the borrowers have to fawn upon the officers and subject themselves to many inconveniences. The relief the government affords is usually very limited in amount and as a financial aid this method is totally inadequate.*

* By virtue of the present charter the Imperial Bank cannot extend its activities in this direction. If however such an extension were to take place in the near future it would certainly help the agriculturists to obtain the needed credit.

The government attempts to lend money under the provisions of the Land Improvement Act but here also the instructions are irksome and exacting. For instance, if land is not encumbered, the land-owner is supposed to possess enough resources; if land is encumbered the land-owner has no good security to offer, thus in either case, the applicants' request is usually turned out. Besides they are essentially of the nature of doles and instead of this the free and normal flow of capital should be the ideal aimed at. This is the A B C of agricultural credit.

As all these methods are defective to a certain extent, the government should undertake to supplement them and the Imperial Bank * should be forced to set up a supplementary system of agricultural finance at almost all its district centres and the government should have a voice in the management of it. It is true that it is not the duty of the state to provide money to assist private enterprise. Sir James Meston remarked that the "land mortgage banks would be of much value to this country. Everybody will recognise that it is a very different sort of institution from the ordinary commercial bank. It must be an institution which is financed very largely by long-term deposits in order to ensure that it shall not be embarrassed in its handling of

* The total advances to agriculturists made in 1919-1920 amounted to Rs. 93,092,764 of this about Rs. 28,633,000 have been repaid to the Government and at the commencement of the year Rs. 64,459,619 were outstanding—*Vide* Finance and Revenue Accounts of the Government of India, 1919-20, pages 335-350.

advances to landlords and estate-holders. It is a type of bank which I do hope to see established in this country; but I hope to see it done in every province, started very largely by local enterprise and maintained under local supervision and control. It is the local knowledge and neighbouring control by groups of intelligent landlords that are going to make the land mortgage business in this country a success and I do not think that it is of any use for government to undertake work of this sort on a large scale."

But certain special features of the Indian agriculturist should be considered. Those who have sufficient landed property and security to be included in a system of mortgage banking are often sleeping partners having no inclination to borrow, while those who do not want to borrow are without any security against which debenture loans can be raised. The deep importance of flourishing agriculture to the state needs no emphasis. The agriculturists are so sunk in ignorance and their methods of life are so different that they fail to make out a case for themselves. It is highly èrroneous to expect that the landlords should do everything for themselves. Taking the case of all progressive countries, special and permanent machinery to faciliatte the provision if long-term mortgage credit for agriculturists have been created. Sir F. Nicholson has divided these institutions into private and public institutions; the latter are chiefly the creation of some local body, whether province, municipality or commune. Germany,

Switzerland, Russia and Denmark possess land banks of this type. In Argentina there is a highly developed system of land mortgage banks and their bonds are known as "cedulas." The German institutions are known as "Landschaften"* and in Hungary they go by the name of the "Boden Credit Institutions". In Denmark they are known as "Credit Corporations". Due provision is made for such institutions in the United States and the Dominion of Canada. Although State-managed land banks may be out of question in our country due to the exigencies of state finance yet the state can do important service in giving the needed impetus for the formation of private institutions of landowners for the purpose of obtaining loans at cheap rates for the members on common security of all.

These banks should consist of land-owning borrowers with a right to claim loan on the security of land at any time. The land is to be valued by duly appointed or qualified appraisers and the loan is to be given in terms of money or of bonds. The loan is to run for a number of years and the borrower has to repay it by easy monthly instalments, or clear off the debts all at once if he has the means to do so. He is to pay the same rate of interest which the bank pays only providing for a small margin which can be spent for management expenses, reserve funds, valuation money, and other necessary fees. Loans are to be given to the extent of half the

* A brief description of their organisation and method of business can be obtained from the "miscellaneous articles on German Banking published by the American National Monetary Commission.

market value of the land and the land itself is the security for the bonds to be issued by the bank. The duty of the borrower is not to allow the land to depreciate in value and deteriorate in capacity. He has to systematically pay interest and the amortisation payment regularly till the end of stipulated period.

In other countries such banks are carefully watched over by the government and due provision is made that the bonds issued by these land banks are honoured by the commercial banks and in the European countries these bonds are reckoned as equivalent to government securities and are valued more because they do not fluctuate like the latter which depend on the glorious uncertainties of political fortune. Practice varies slightly in the various cases of the European land banks. Some have share capital, some accept state aid and some admit well-wishers who have to take shares. These are all matters of interesting detail but the main lesson of these institutions is the elimination of all chances of conflict between the borrowers and lenders of these institutions. Their object is cheap credit. Collective guarantee with excellent security is their basis of operation. Vigilance and control are their only proper safeguards. There is provision for compulsory amortisation. Land mortgage banks that work on these lines are essential for our agricultural prosperities.

Some people think that co-operative land mortgage credit is a sordid and unpleasant task devoid of all moral and higher education, and they deprecate

all attempts towards the starting of these institutions. But sentiment should not be guide in such a vital matter as this. Our agriculture needs considerable development so as to be able to furnish the needed food to our increasing population. Co-operative land mortgage is one method which leads towards the perfection of agricultural credit.

But the great difficulty is the inertia which is the characteristic of our people. But for government help and indirect persuasion the co-operative movement would not have shown such remarkable progress. Even now the prevalent opinion among the masses is that the co-operative societies are government institutions financed, endowed and worked by it. No other influence except that of the government can give the needed fillip at the start and no other body can exert such profound influence as the government itself. The landlords must be willing to combine for the purpose of obtaining cheap credit. The government has to favour an organised system of land mortgage credit. An efficient system of land transfer and land registration should be established. Privileges about execution and foreclosure as are enjoyed by the lands-chaften should be granted to these land mortgage banks. State guidance and supervision are needed, and if they are forthcoming the landlords would be willing to take advantage of this new form of co-operation.

The Government of India has inaugurated a policy of agricultural development. Their researches and their practical demonstration of improved methods of farming are steps in the right

direction. But they must also provide the needed credit for the agriculturist who is now in the throes of poverty.

Co-operative land mortgage banks are needed to supplement the existing co-operative credit societies and working together they may be able to successfully tackle the problem of our agricultural indebtedness. These should take full advantage of the work of the government agricultural department and use their influence to improve husbandry and devote funds for experimental purposes.

Easily obtainable credit is not the sole panacea for the numerous ills of our agriculturists. Credit is an important factor but solution should be sought in other directions to solve the complicated problem of our agricultural indebtedness * but these lie beyond the province of the banker.

* As Sir Daniel Hamilton says the Indian ryot carries " a mounthain of debt on one shoulder and a mountain of illiteracy on the other shoulder. One way of benefiting him is to educate him and teach him the powers of organisation and he would be able to solve his indebtedness question. As B. A. Collins says the two chief remedies are—education and organisation. Other remedies like improved methods of agriculture and growth of industry may also help him.—*Vide* B. A. Collins, Indian Co-operative Studies, p. 25.

CHAPTER VIII.

THE INDIAN POST OFFICE SAVINGS BANKS.

Brief History.

The existing system was a gradual development out of the "Government Savings Banks" which were started in the Presidency towns between the years 1833-1835. This system was extended to certain selected districts where they were instituted in connection with the district treasuries. A uniform type of these savings banks was introduced in all other parts of the country in 1882 and 1883. These absorbed the business of the district savings banks in 1896.* "From that date forward these savings banks have been managed by the postal department. No special reserve is maintained against these deposits. The deposit money constitutes what is known as the 'unfounded debt,' and is a floating charge on the credit of the government. The deposit money † is utilised for capital expenditure. Although there may be a run on these banks the government can meet it without any great difficulty.‡

* The fifth Decennial report of Moral and Material progress in India, page 302.

† The greater the deposit money the greater is the claim on the general resources of the government.

‡ At the outbreak of the recent war there was such a run. Even the Paper Currency Office was raided by note-holders for conversion purposes.

Object

The chief object with which they were started was to inculcate the habit of thrift among the middle and lower classes of people. Direct encouragement to investment is given by the granting of interest (3 per cent. on call deposits and 3½ per cent. on fixed deposits). The limit up to which an individual depositor can place money is rupees 750,* within the course of a year. The individual amount of deposit cannot be more than rupees five thousand. The Government gives the depositor the option of converting his money into Government paper if he so likes.

It has been calculated that hardly 15 per cent. of the depositors are agriculturists. Only the intelligent middle-class people avail themselves of these banks and the low rate of interest offered is not a great inducement sufficient to compel them to retain their savings here. Mortgage and pawn-broking business pays more and the ladies of wealthy families and the monied lawyers utilise their savings in this lucrative business. So long as mortgage banks specialising in this particular line are not started the investment of savings in these banks or the Joint Stock Banks cannot be expected to grow apace. The possession of land confers peculiar social status and much money is invested

* Up till the year 1912 the deposit limit was Rs. 200 then it was raised to Rs. 500 but now the maximum deposit money is Rs. 750.

in the land mortgage business. So long as these habits dominate it is hard to expect any increase in the banking habit of the people.

Sir H. B. Smith's Committee writes " we are impressed by the comparatively insignificant figure of the total deposits in the post office savings banks amounting to only Rs. 24½ crores on 31st July, 1914, before the conditions that ensued on the outbreak of war led to the heavy withdrawals. We understand that the substantial increase in deposits in the years 1912-13 and 1913-14 amounting to over four crores was due mainly to the grant of additional facilities and we recommend that the Government of India should examine how far notwithstanding the admitted administrative difficulties it may be possible to improve the present procedure for the deposits and withdrawal of money and to increase the number of post offices conducting savings bank business."*

The bankers interest in the matter of the P. O. Savings banks does not confine itself only to their deposit-attracting function. These banks facilitate the transfer of small sums of money from place to place by the money order system. The Government follows the well-known clearing principle in the matter of this business. It sets off payments in opposite direction against one another and thus obviates the necessity of sending coins or currency notes. As a matter of practice it has realised that amounts remitted to and from a town very often

* *Vide* Sir H. B. Smith's Committee report, page 82.

balance one another during the course of the week.* The Government also provides for telegraphic money orders; Rs. 600 being the maximum limit up to which they can be issued. These T. M. O.'s must not include fraction of a rupee. The ordinary fee plus a telegraphic fee is charged.

Suggestions

More concessions as to the withdrawal of money say twice a week, the raising of the maximum amount of deposit money from Rs. 750 to Rs. 1,500 and the issuing of more pass books in vernacular to those who desire it should be made. A higher rate of interest should be offered. The present rate of interest was fixed long ago when the government borrowed at three and half per cent. The government should realise that the value of money has gone up enormously. The government is at present borrowing at 6 per cent. and the post office cash certificates which are issued at a liberal rate of interest running practically at compound interest are detracting the popularity of the savings banks. It is indeed bad statesmanship to pay 3½ per cent. to the poor and middle class depositors

* The present fee for sending ordinary money orders is graduated as follows; on any sum not exceeding Rs. 10 is annas two, on sums exceeding Rs. 10 but not Rs. 25 the charge is annas four, on sums of rupees 25 and if the remainder is less than Rs. 10 the charge is annas 2 but if it exceeds Rs. 10 the charge is annas 4.

while it pays five to six per cent. to the richer people who lend money to it.*

Every treasury and sub-treasury should be utilised as a savings bank and empowered to deal with current accounts. The savings bank system should be energetically pushed throughout the country by opening more post offices. The money that is collected by the P. O. savings banks should be utilised for the local needs of the district. The government is making an organised effort to increase public interest in the sale of the post office cash certificate. This sale is ultimately bound to give great stimulus to thrift and the systematic encouragement of this habit will have profound influence in bettering the future economic condition of the people. A portion of the money obtained by the sale of these Cash Certificates in the district and rural areas should be set aside for use in those rural areas.

These savings banks encourage savings but like the co-operative credit societies they do not create wealth by productive employment. They not only promote thrift but increase the wealth of the society, hence they have been styled "perfected savings banks.[22]

The progressive model of the postal system of the countries like Austria Hungary or the Swiss Republic is not copied here. The development of the postal cheque system is necessary. The government

* In other countries the savings deposited in the postal savings banks also increased along with the deposits of other banks, but in India on the other hand the deposits of the postal savings banks have not increased as a higher rate of interest has not been offered.

should open postal cheque offices and permit individuals to open an account at these offices with a permanent deposit of about Rs. 100. This can be operated through any post office in the country and money transmitted to any other part of the country without limit of amount. Of course a moderate charge can be levied in this case as in the case of the money order system. In a big country like India where banking is so imperfectly developed, a system of this kind will make money fluid and as Mr. Darling suggests they would be of the greatest advantage to co-operative societies to whom the transfer of money is often a matter of considerable difficulty.

Table showing the growth of deposits in the P. O. Savings Banks :—

Year	Number of Depositors	Deposits Rs.	Interest Rs.	Average balance of deposits Rs.	No. of Post Office Saving Banks.
1900	786,000	37,597,000	2,827,000	123	...
1905	1,095,000	55,523,000	3,812,000	125	...
1910	1,379,000	60,021,000	4,477,000	115	...
1914	1,639,000	116,037,000	6,191,000	141	9,824
1915	1,644,000	96,062,000	5,394,000	91	10,161
1916	1,666,000	81,632,000	4,320,000	92	10,386
1917	1,647,000	93,822,000	4,547,000	101	10,421
1918	1,638,000	111.669,000	4,440,000	101	10,925
1919	1,677,000	134,511,000	4,687.000	...	10,670
1920	1,760,442	177,451,171	—5,646.213	...	10,713
1921	1,877,957	188,485,138	—6,219,740	...	...
1922	...	...	...	...	...

CHAPTER IX.

Co-operative Banks.

The chief object of this chapter is to show the structural differences between a co-operative bank and a commercial bank and the different methods of procedure adopted by them. As the report of the Government Committee on Co-operation in India has shown " the same basic laws of finance govern both ordinary and co-operative banking." *

Co-operative banking in India is in its infancy. It may without exaggeration be said that it had not yet had time to evolve a systematic and definite policy of its own. The co-operative mind is still oscillating between long-term and short-term loans. The way in which the administration of a reserve fund, is to be conducted has not been positively laid down. The problem of securing adequate financial help has not been satisfactorily solved as yet. The question of obtaining access to the money market to permit the provincial banks to unload their seasonal surplus, or borrow funds by rediscounting the co-operative paper or by a system of cash credits from the hands of the Imperial Bank or other commercial banks, the starting of an all-India Co-operative Bank, the formation of an all-India Co-operative Union to improve the co-operative backwardness of India by

* MacLagan Cofmittee's report on Co-operation in India,—1915.

consolidation anr federation of theexisting co-operative societies, the subject of co-operative education, the important issue of the future attitude of the government towards the co-operative movement, the problem of relieving the overburdened registrars and the trainink of co-operative workers and office-bearers have to be effectively dealt with and a satisfactory solution of these problems would improve the organisation and increase the momentum of the co-operative movement in India and will bring India into line with other countries of the co-operative world. The central banks should realise the purpose for which they are designed. Though the absence of propagandist bodies is forcing the central banks to confine their attention to propaganda, organisation, education, and supervision of societies yet they should realise the truth of Mr. Wolff's remark "the central bank is when all has been got shipshape, to serve not to be tutor to the local banks. It is in fact designed to be a bank." Similar other problems have yet to be solved but the co-operative movement has taken a firm hold of the people and as Mr. Wolff prophetically remarks "the movement is bound to become a permanent asset of immense value to India."*

It is imperative to recognise the vast difference that exists between a co-operative banking institution and the commercial bank. The business of a bank is to create credit, and place it in the hands

* Mr. H. W. Wolff, Co-operative Credit Movement in India, pp. 344-45.

of the deserving people of the community. It is to act as an intermediary between the lenders of money and its borrowers. It collects small savings and turns this broad stream to fertilise and irrigate the channels of industry and commerce. It grants loans on the strength of adequate security entrusted to its hands. Occasionally it permits people of undoubted personal security to overdraw their accounts now and then for a short time. It discounts bills of exchange arising during the course of trading transactions and by purchasing the trade bills it grants the needed money to finance trade. This briefly speaking is the work of the commercial bank which is familiar to everybody. It brings prosperity to all parties concerned in the matter but unfortunately it makes the rich richer and in no way benefits the poor man and does not uplift him to a higher scale in the society. Only a few fortunate rich can satisfy the exacting requirements of a commercial bank in the matter of security but the poor by virtue of their poverty are handicapped. It is here that the co-operative bank comes up to fill the gap. The co-operative bank is the poor man's bank or people's bank as learned writers put it. Its main duty is to democratise credit and place it in the hands of the poor who though they may be entitled to credit scarcely get any recognition at the hands of the commercial bank.

The co-operative bank acts not only as an intermediary between the lender and the borrower of money but it tries to inculcate principles of thrift. In the process of obtaining credit from the

co-operative bank there is edusation. As M. G. Francois has written "the co-operative banks democratise credit, relieve distress, create wealth and turn to good account industrial and agricultural opportunities." The hitherto isolated people learn the value and powers of association. In the very methods of providing credit the co-operative bank teaches the lessons of self and mutual help and suggests the extension of these to outside matters other than credit and thereby promotes insensibly their own self-development.*

The commercial bank is a Joint Stock Bank where the manager plays an all-important part and the shareholders are sleeping partners. On the other hand the co-operative bank resembles "a piece of active machinery in which every spring, every wire is alive and knows and conscientiously performs its duties being endowed with the capacities of rendering discriminately service according to the merits of each case watching and checking the other parts." There is common control and wide publicity and efficient supervision in the co-operative bank. There is a sense of responsibility in the minds of each member. There is discrimination in the selection of loans. Utmost vigilance is exerted in the control of their employment. Thus there is much of self-education in this case. The co-operative bank has

* In the direction of sale and purchase societies to benefit agriculturists and town dwellers, the financing of cottage industries and the solution of the housing problem a humble start has been made in this country and the cementing bond of co-operation would soon pervade every activity of our social life.

certainty of custom and a well-known market. The quality of customers is all that is desired because the "customers have passed through the sieve of selection and having been tried and approved are held fast by the powerful bond of Joint Stock interest and common liability." The commercial bank has no such advantage.

The co-operative bank operates with small working capital and insists on prompt and easy payments. It succeeds in turning over its money with comparative rapidity, the co-operative bank takes special safeguards to protect itself against the bad debts. They are the linking-up of the liability of all and the insisting of the productive use of money that is lent. The co-operative bank is near and familiar while the commercial bank is distant and unfamiliar to its customers.

The co-operative bank is a successful "tapper" of savings. It affords a better rate of interest to the people. There is more remunerative employment of its fund than in the case of the government post office savings banks. These are subordinate to the government. Like the co-operative banks, the savings banks do not educate and train savers to independence and enable them to obtain business knowledge and promote self-reliance on their part. "It is not self-government." A co-operative bank is the depositors' own bank and here "the money may be profitably employed in setting up workmen's dwellings, in settling small folk on land and money is made to fructify in productive employment."

There is no antagonism between the two kinds of banks, one seeking to destroy the other or planning for the downfall of its rival. There is a place for both these kinds of institutions in a well-organised credit system. The commercial banks hold the cash box of the market and have full control over the money market. The co-operative banks do not wish to dethrone them from this position. They wish to play a less humble role as "collecting" banks and not as rivals but as "feeders" endowing small peoples with moderate capital and train them to banking habits and prepare them for business with more capitalist institutions to which they are likely to go as they become wealthy. They educate and train the people towards habits of thrift and draw money out of hoards. This is the philosophy of co-operative banking as explained by one of the greatest of its living apostles—Mr. H. W. Wolff.

While such has been the idealistic aims of the true co-operators who are guiding the co-operative movement it would be interesting to note how far these ideas have been realised in our country.

The co-operative credit movement was first started in 1904 to "encourage thrift, self-help, and co-operation among agriculturists, artisans and persons of limited means." The scope and area of this movement was extended by the Co-operative Societies Act of 1912. To-day there are a great variety of types among the credit societies. The money doles extended by the government in the early stages of these societies have been discontinued. In the matter of audit and supervision, training and

propaganda, non-official support is being actively enlisted. Annual conferences of Registrars are thrashing out the different problems attending on the course of their daily routine of business. More societies are arising. Members are increasing. The capital of the society is fast increasing and though a crisis in one province or a failure in other places may occur the movement is having a healthy progress. The following table indicates the rapid growth of the movement.

*Table * showing the growth of co-operative societies.*

Year.	Number of Societies	Number of members	Working capital (Rs. 000 omitted.)
1905	41	..	1
1907	843	90,844	23
1909	2,008	184,899	80
1909	5,432	314,101	203
1913	12,324	573,536	534
1915	16,324	824,469	896
1916	19,675	918,436	1,032
1917	23,036	960,960	1,222
1918	26,465	1,061,764	1,440
1919	32,439	1,235,891	1,755
1920	40,772	1,521,148	2,140
1921	47,503	1,753,000	2,643
1922	52,182	1,974,000	3,112
1923	56,136	2,102,000	3,554

While the above table speaks of growth of the co-operative societies of all kinds the following table shows that there is progress in the growth of

* This table is from the statistical blue book relating to the co-operative movement in India—1922-1923. The average membership per society is 37—Capital is increasing faster than membership being nearly Rs. 169 per member. The capital per society is Rs. 6,331.

non-agricultural societies, the central banks and the guaranteeing unions as well.

	1919-20	1920-21	1921-22	1922-23
1. Central (including Provincial and central bank and banking unions).	400	449	480	514
2. Supervising and guaranteeing unions.	994	1,150	1,240	1,379
3. Agricultural (including cattle and insurance societies).	36,716	42,582	46,788	50,286
4. Non-agricultural.	2,662	3,322	3,674	3,957
	4,0772	47,503	52,182	56,136

While rural co-operation has made such rapid strides yet many of its votaries are not satisfied of this astonishing growth. Sir D. Hamilton says "that we have 700,000 villages in India and what a small fraction of them have been benefited. At the present rate of progress we still have to wait until the year 2200 before every one of them has its own bank." Mr. H. W. Wolff reminds us that "Rome was not built in a day" and if it had been it would not have become the "eternal city." He advises caution, safety, and enduring success. Better management of the existing primary societies checking the evils of unpunctuality in the payment of loans and the baneful practice of making book adjustments and taking benami loans is far more important at the present stage than the mere growth of many unstable societies. As Sir D. Hamilton says "the country is still in the grip of the mahajan." Mr. Wolff* says "it is the bonds of debt which shackle agriculture. It is usury, the rankest, most extortionate, most merciless usury—which eats the marrow out of the bones of the ryots and condemns

him to a life of penury and slavery, in which not only is economic production hopeless but in which also energy and will become paralysed and men sink down beaten into a state of resigned fatalism from which hope is shut out and in which life drags on wearily and unprofitably as if with no object in view. There is no use denying the fact—it is plain to all eyes." Now that his two Richmonds "thrift" and "modern credits" have been created by the co-operative movement it would take some time to solve the present indebtedness of the agriculturists. The poverty problem is a wider one and although indebtedness is one cause for poverty yet its extinction would not remove the basic reasons for the poverty of the agriculturists.

Another strong reason why these co-operative banks should be encouraged is that their deposits are of a " lying character."* As Mr. N. D. Beatson Bell says " the co-operative banks have weathered the crisis when many of the " swadeshi " banks failed. They have weathered the crisis when the greatest war in history began and they have weathered many a storm already and in spite of these trials the co-operative credit movement is going strong." Mr. J. N. Mitra says " while withdrawals from the post office savings banks were fairly large and although there was a run on the Indian Joint Stock

* About 50 per cent. of the capital of the co-operative credit societies consists of shares contributed by its members and ten per cent. consists of deposits by the members and the remainder consists of commercial credits.

Vide Strickland, India of To-day, Volume I.

Banks " there was hardly any rush on the co-operative banks for deposits and this means the public has a good deal of confidence in the movement." It is these banks that can best tackle with the hoarding tendencies of the agriculturists. The employment of systematic collectors or home boxes to tempt people to put money in them would lead to the formation of the deposit habit. These methods have been tried with success in America and bid good promise in our country also. The co-operative banks are already acting as compulsory savings banks and in many districts in India, the cultivator deposits his money after the harvest time. This practice should be stimulated and when once the agriculturists is broken to thrift there is prosperity in store for him.

Besides these Economic benefits of the co-operative movement the social, moral and educative effects which can be reaped as bye-products are very many. Mr. J. N. Mitra says " instances can be multiplied to indicate the indirect effects of the movement, how it promotes the moral and social improvement of the people, brings about reformation of bad characters, creates a desire for education, encourages the settlement of village disputes by arbitration, discourages litigation, promotes a wider outlook on life and makes village life healthier in all its relations." Speaking of the utility * of co-operative activity Mr. Wolff says " there has indeed never

* A tacit recognition of this led the French government to grant ten million francs for the reconstruction of co-operative societies in the war-ravaged territories.

been a Midas-like touch of this beneficient power nor so fruitful a generator of popular education, stimulating with the growth of worldly possessions, the thirst for knowledge and the longing for higher treasures and knitting people together by a community of feeling into an enlarged family.*

* H. W. Wolff—Rural Reconstruction.

CHAPTER X.

THE NEED FOR BANKING REFORM.

The existing banking system of India needs thorough reform. There is hardly a banking system worth its name. The several component banks do not remember their close affinity of relations and extend mutual sympathy and help. India does not possess "a close-knit banking organisation" as in the case of Germany, Japan, France, or the United States of America. This absence of thirst for system or wholeness or close-knit organisation is chiefly due to the tendency of the Indian banks to do business "each for itself." The Imperial Bank, the exchange banks and the Joint Stock Banks work severally and not collectively. The Exchange banks have striven hard to protect their business from competition with the Imperial Bank.

The Indian Joint Stock Banks copy the tendency of the English Banks which justify their existence solely on the ground of profits. They aim at becoming commercial bankers having no connection with industrial finance. It is true that short-term loans are granted to industries but they never sacrifice the principles of safety and liquidity of assets which commercial banks have always to keep in view. But commercial banks alone will not create the needed credit for our agricultural and nascent industries. New banks should arise to satisfy the

needs of agricultural and industrial credit. Just as the co-operative credit movement is borrowed from Germany, the German feature of close relationship between industry, finance and transportation is also worth imitation. Indian economic development cannot be fostered unless there is a close alliance between banks and industries as in the case of Germany * or Japan. Either new industrial banks having nothing to do with short-dated deposits should arise or the existing banks should take up industrial financing under proper safeguards.

That the Indian joint-stock banks have borrowed, copied and translated the chief features of the English banks is an undisputed fact. They have copied the tendency of the English banks in having huge authorised capital, a part of which is subscribed and out of which very little is paid at the beginning Like the English banks they wish to trade largely on credit. The Government of India has followed the British Government in their *laissez-faire* policy in the matter of banking business. Imitation for imitation's sake has produced unworthy specimens. The superficial elements alone have been copied while the really vital and progressive features of English banking have not been engrafted on our

* The German banks do not aim solely at profit but consider the development of their industries as an important duty. One German Director giving evidence before the American N. M. Commission says that the " One difference between the banks of England and Germany is that in England the primary purpose of the banks seems to be to secure large earnings for their scholarships; in Garmany our banks are largely responsible for the development of the Empire and have built up its industries.

system. Bankers' associations, bankers' institutes* and guilds have not been created on the English model. The Imperial Bank does not possess the traditional glory, respect and power enjoyed by the old Lady of the Threadneedle Street in the London money market. There is a note-worthy absence of control either by the Government or by a banker's association.

Again a part of the financial system alone has been imitated. The Indian banks are merely pursuing commercial banking. In England besides banks, there are trustworthy promoters, capable underwriters and issuing houses so that industrial companies derive invaluable aid from them. It is but natural that the Indian industrialists would look forward to their banks for this kind of business also owing to the absence of these specialising concerns.† India made an unwise choice in selecting the English banking system as her prototype. The progress of

* The British Bankers' Association in which is merged the English Country Bankers' Association was started in 1919 to look after special questions affecting banks. The British Overseas Banks Association consists of the British banks having a London Office. This was started in 1917. The Institute of Bankers, London, the Scotch Institute of Bankers and the Institute of bankers in Ireland are formed mainly to facilitate the discussion of matters of interest to bankers. *Vide* Sec. on bankers association in Chapter XI.

† In the absence of these agencies the industrial companies find it difficult to obtain loans. Industrial investment practically comes up to locking up of money at present. Our stock exchanges do not facilitate the quotation of a new company unless the promoters are well-known. The stock exchange brokers have a few favourite scrips and any amount of skilful manipulation in their value is done in accordance with the Bull or Bear tendency of the times.

Japan is solely due to her selecting the salient features of merely every banking system in the world and engrafting them on her own banking conditions. The specialising tendency visible in the English banking system is noticeable in Japan. It has imitated the model of the French banks. It has copied the useful branch bank system. It has borrowed the continental system of close relationship between the small banks and the central bank. It has encouraged the co-operative credit societies. It committed the mistake of imitating the U. S. A. National banking system and after a short trial it gave it up for the central banking system with the Imperial bank of Japan as the crowning head of the banking edifice. The whole credit system was thoroughly organised by banking experts borrowed from foreign countries. State help and control enabled the banking system to work well.

The Indian banking system should be thoroughly overhauled and reorganised on an improved basis. The materials already exist. The exceptional position, unrivalled organisation and vast knowledge of the Imperial bank should be utilised and it should be made the keystone of the whole arch. The other banks should know definitely the help they can expect from this Central Bank. Agrarian, industrial or commercial credit both for short period as well as long term purposes should be created by the existing banks or fresh ones that will arise in the near future. The Government should see that there is no abuse of the word " bank " as in the past and by restraining legislation smooth the progress of the banks.

An attempt should be made to profit from the experience of the continental countries by copying all their deserving features. The English banking model is not the best model nor is it suitable to our present needs. Mr. Keynes was quite correct when he wrote that England's was the worst currency model that India could imitate. Even in the matter of banking business the Indian people should realise that their salvation lies in selecting the salient features of all banking systems and adopt them as Japan has done.

The existing Indian banks can be divided into three classes, *i.e.*, the Imperial bank with its close relations with the Government of India, the immigrant banks and the local Indian Banks. The Imperial bank finances the internal trade to a great extent by discounting commercial bills. The immigrant banks develop the Indian trade with their own countries and naturally assist their own countrymen. It is only with their surplus money that they give help to Indian industries carried on, on a large scale. The local banks imitate the Imperial bank and conduct commercial banking. Sometimes they lend money on Zemindary properties in preference to Industrial securities.

Many of the banks are managed by foreigners who come only into contact with "a few of the aristrocracy" and so ordinary traders and small industrialists do not receive much help from them. So they have to pay high rates of interest for any accommodation they may get from the public and sometimes thriving industries suffer from

insufficiency of capital. Industrial financing is not on a sound and proper basis.

The financing of rural trade and credit is not properly designed. The existing banks do not care to change the present methods of rural credit. It is growing more evident day by day that the present insufficiency and waste involved in our export trade business should be rectified as early as possible. Our export trade is left to the mercy of funds outside the country. As in "capital poor countries" our export trade is financed by the importing country to a great extent. The big export and import houses are in the hands of Europeans who employ their agents to collect the produce from the interior and send it to the Port stations whence they are shipped at their own risk and cost. The agents necessarily finance the cultivators from the beginning and the crop is hypothecated to them.

This system of financing our internal trade for exportation purposes is not to our best national interests. The chief harmful result of this process is that the foreign merchant houses are exploiting our agriculture in their own interests. Export of rice and wheat is increasing while their production is not on the increase at all. Cotton and jute cultivation is increasing while food production is not progressing satisfactorily. The production of non-food crops for export purposes is chiefly due to the influence of cash advances of the foreign merchant houses. Thus our economic prosperity is mainly dependent on these firms.

This system of exploiting agriculture in the interests of foreign exporters should be given up. The introduction of Co-operative credit societies combined with co-operative sale societies will go a long way in remedying this state of affairs. The question of removing this rapacious middleman requires patient tackling for a long time.

The system of financing our international trade is equally unsatisfactory from the national point of view. The exchange banks are financing our trade bills and every one of them has its head office in the European countries, or Japan or America. They have steadily taken up the financing of our trade with their countries. They display no desire to ake part in the economic reorganisation of our country. They have no ambitious national programme for India's uplift. These banks remain distinctively foreign much the same as they were at the start. They are more willing to help their own countrymen and trade with European business firms and are not anxious to attract the accounts of small and new firms started by the Indian people. An Indian firm rading under a European designation is more fortunate in obtaining accommodation from the existing banks.* These are some of the drawbacks of the existing powerful banks. On the other hand it is also true that the Indian managed companies sometimes fail to exhibit their financial position in a business-like manner to convince the European manager as to the safety in

* *Vide* Mr. Manu Subedar's evidence before the Sir H. B. Smith Committee. Also the evidence of Mr. D. P. Khaitan before the Indian Fiscal Commission.

granting loans to them. Although the co-operative movement has already become an important wheel in the financial machinery of this country yet its importance has not been sufficiently realised by the Government or the other members of the money market. As the deposits of these banks are increasing and as they have to hold gilt-edged securities against them the finance member should realise that there is an expanding market which will enable the Government to obtain more finance for productive works in the coming future. Increasing use of notes and cheques can be brought about by the co-operative banks as the landlord, the Bania and the Mahajan begin to deposit their savings in them. The finance minister should count on these immense potentialities instead of relying on the unstable deposits of the savings banks. An attempt should be made to fit in these co-operative banks into the financial machinery of the country so that the surplus funds of the money market during the summer season might be safely lent through the co-operative banks to finance the agriculturists just at the time when they require it. The present system of water-tight compartments of rural, Government and commercial finonce is essentially backward and is a relic of the older times, that should be swept away at the earliest moment. The first step in the reorganisation of the financial machinery of our country has been achieved by assimilating Government finance with the commercial financing agency and what is required at present is to forge a strong, lasting and desirable link between the three systems so that equilibrium

of monetary demand and supply can be achieved with comparative ease.

It is indeed high time that our banking system should be reorganised on a healthy basis giving scope for the proper mobilisation of our money. The healthy development of our trade, the careful promotion of our industries, a wise economy of our precious metals and the real increase of our national wealth—these are the problems that a soundly organised banking system has to solve.

CHAPTER XI.

BANKING REFORM.

1. *More Banking Capital.*

The first striking feature of the Indian money market is the smallness of banking capital or loanable money. A notable demonstration of this fact is visible every year in the rise of the bank rate during the busy season. "Though the average bank rate is not high still the maximum figure to which it rises is a high one." Though the Imperial Bank has appreciably lowered the average bank rate to five and a half per cent., yet the bank rate rises to nine per cent. during the busy season. Another noticeable feature is the wide fluctuations in the Indian Bank rate. While all progressive countries of the civilised world try to maintain a low bank rate and consider its raising as an unavoidable necessity due to acute stringency, India has become accustomed to these wide fluctuations which have almost become an integral part of her banking system.

Financial facilities are an important desideratum at the present time in this country because a new era is setting in. Capital is required for the financing of new railways, developing forest wealth and constructing public works of a reproductive character. The economic development of our country would be seriously handicapped if sufficient capital is not available. "Money is the Alladdin's Lamp which

creates everything at will." The extension and development of the existing industries require a huge amount of capital. Thanks to the war, the activities of the Indian Munitions Board has manifested to us various new directions in which capital can be profitably utilised.* The agriculturists, demand for capital has also to be reckoned. The funds for the financing of our foreign trade should be taken into account and the total demand for capital under all these items would amount to a respectable figure† The internal trade of the country is certainly five to ten times larger than the external trade‡ For an adequate financing of these varied interests sufficient capital is needed.

The amount of loanable capital that lies at the disposal of the Imperial Bank, the exchange banks and the joint stock banks falls short of the required figure. The following table gives a rough idea of

* A number of new schemes to harness the waterfalls of the Western Ghats, the smelting of zinc and copper and the production of sulphuric acid on a commercial scale, the treatment of coke bye-products and the production of heavy chemicals and aniline dyes, the manufacture of textile machinery and mill accessories, the building of steel and oil engines are some of numerous industrial activities that are contemplated by the organisers of India's Industrial development.

† According to Professor K. T. Shah our capital requirements would amount to 1,000 crores of rupees.

‡ The internal trade was computed at 1,597 crores in 1919-20 and 1,497 crores for 1920-21 and 2,000 crores for 1921-22. As Professor Fisher says " the internal trade cannot be more than the amount of produce available for exchange." In India a great number of middlemen intervene between the producer and the ultimate consumer of goods. This leads to greater frequency of transfer of goods from hand to hand. The official method of calculating is to consider the amount of our produce once as exports and once as imports and the total figure is considered as the amount of our internal trade.

the strength of the different banking systems of the world.

Countries.	Banks.	Branches.	Paid-up capital.	Deposits.	Exports.	Imports.	Population.
			('000,000) omitted*				
Canada	18	4,865	$129	$2,225	$1,189	$1,240	8
Australia	18	2,795	£50	£288	£127	£103	5
The United Kingdom	8	6,915	£123	1,813	£1,334	£1,932	47
Japan	2,052	4,889	Y1	Y9	Y1,948	Y2,33[illegible]	56
U. S. A.	30,000		$1,413	$15,000	$8,080	$5,278	105
India	87	380	£1	£20	£189	£239	247

It is a well-known fact that many metropolitan banks of London possess more capital than all the Indian Banks put together as shown in the following table.†

Name of the Bank.	Capital and Reserve.	Deposits.	Branches
	In £ (000) omitted		
Barclay's	23,742	303,186	1652
Lloyd's	24,373	330,557	1613
London Westminster and Parrs	18,008	280,820	892
London Joint City and Midland	21,720	354,406	1670
National Provincial and Union	18,399	263,037	1070
	106,152	1,532,006	6,904

So the outstanding fact is the smallness of the capital and the size of our banks. Sir Norcot Warren while placing the scheme of amalgamation

* These figures relate to the business of the banks in 1920-21 and are compiled from the official year books in the case of Japan, Canada and Australia and the Statesman's year book in the case of the U. S. A. and the statistical tables relating to banks in India, and in the case of the United Kingdom the Bank of England, and the Big Five alone have been taken into account.

† This table relates to the business of the " Big Five " in London. The figures are taken from the bank account published in the Journal of the Institute of the Bankers, April, 1923, page 211.

of the Presidency banks before the shareholders of the Bank of Bengal openly admitted this weakness of our banking system. The proposed amalgamation, he says, means "added strength and more capital to our banking system."

More loanable money should be at the disposal of the banks. As Mr. (now Sir) M. DeP. Webb says "India needs more banks manned by *Indian* men and furnished with *Indian* capital." It must be admitted that our banks have realised this fact and some of the more progressive banks are increasing their capital in order to provide the needed credit facilities in our money markets. This increase of banking capital can be considered as an indication of the stability or financial capacities of the banks. Banking enterprise is thus provided with fresh scope for its activity. It is a matter of increasing gratification to find that the Indian depositors are confiding more trust in the existing banking institutions. At any rate the Indian people are now slowly realising that "without banking capital there can be no credit and without credit the primitiveness of barbarity would remain."

1. *Table denoting the Increase of the Paid-up Capital of the Banks.*

(Figures Rs. 000 omitted.)

Name of the Bank	1918	1919	1920	1921	1922
The Bank of India ...	5,000	9,909	10,000	...	...
The Punjab National Bank ...	1,645	1,659	1,853	...	...
The Bank of Baroda ...	2,029	2,041	2,412	...	...
The Central Bank of India ...	2,500	4,990	5,000	...	...

Name of the Bank	1918	1919	1920	1921	1922
The National Financing and Commercial Corporation.	1,066	1,089	4,000	...	...
The Bombay Merchants Bank	471	471	1,000	...	
The Bank of Mysore ...	1,000	1,000	1,932	2,000	...
The Bangalore Bank ...	440	455	548	...	...
The Punjab Sind Bank ...	322	326	376	...	...
The Nedungadi Bank ...	304	360	434	...	...
The Muffusil Bank ...	199	300	400	...	...
The Tata Industrial Bank ...	7,001	15,181	15,178	22,379	22,673
The Vellore Mercantile Bank	177	371	409	...	...
The Bank of Behar ...	113	130	176	...	...
The Allahabad Bank ...	3,000	3,000	3.000	...	...
The Alliance Bank of Simla ...	8,682	8,808	8,851	...	...
The Indian Bank (Madras) ...	1,000	1,000	1,000	1,000	1,259

Some of the Eastern exchange banks also increased their capital but how much of it is being employed in India cannot be definitely ascertained.

2. *The Banking Habit.*

The Indian people have not yet acquired the banking habit. They require education in the economical use of gold they possess. They must bear in mind the advice of Adam Smith that " coinage is unproductive capital, it does nothing but pass from hand to hand and is not put to any useful purpose whatsoever."* As Sir D. Hamilton says "The gold sovereign is a cheque drawn on Europe " and there is no use of hoarding it or locking it up in the family vaults for safety's sake. They should realise that hoarded wealth does not increase their economic well-being.

One of the chief causes hindering the growth of capital in India has been said to be the hoarding habit that prevails among the majority of the

* Adam Smith, Wealth of Nations.

people. One school of thought points out that India cannot accumulate an appreciable amount of capital because of her hoarding habit. India has been designated by one historian as the "land of fabulous hoards." One economist calls India "a sink of precious metals." There are others who speak of vast hoards which exist in India. Mr. H. D. MacLeod was the first economist who started the theory of hoards and ever since that time the hoarding problem has almost become classical. He estimates the amount of Indian hoards at £300 millions. Lord Curzon says "the whole hoarded wealth of India amounts to over Rs. 825 crores. Think of all this money lying idle or at most put out for usury or relatively unproductive forms of investment."* Mr. Arnold Wright estimates the amount of Indian hoards at £700 millions.†

Opposed to this school of thought there is the popular school which attributes the shortage of capital to the annual drain of money by way of home charges. This school emphatically denies that these annual drains leave capital to accumulate in India. As Dr. A. Marshall would say capital can grow from the surplus of national income over national expenditure or in other words net national dividend. Any untoward call which decreases the national income contributes towards the decrease of the national dividend. The annual drain reduces the national income considerably and hence the national dividend is

* *Vide* Lord Curzon's speech at the Bengal Chamber of Commerce Jubilee in the year 1903.

† *Vide* Financial Review of Reviews, Dec. 1916.

correspondingly reduced. There is no legitimate ground for grievance so far as the home charges are direct payment for services rendered to India but an appreciable amount goes away from our country as profits of industries managed and financed by Europeans. Here is the legitimate ground for complaint. The first and foremost duty is to stop this invisible drain as it is styled by insuring a rapid growth of capital in India. Artificial attempts for the nationalisation of foreign capital have failed everywhere and it is unwise to raise artificial restrictions against the free flow of foreign capital.* It is the paramount duty of every citizen who can save from his income to rid her of the domination of foreign capital and obtain control of all the vital industries in our country. As Lord Curzon says "a country is in the strongest position whose capital is self-generated and self-employed."

Coming to the question of our fabulous hoards it is hard to reconcile certain economic facts with the statement that India has "fabulous hoards." The first statement which gives lie to the theory of hoards is the extreme poverty of the people and the very low standard of living that is implied by it. There is no appreciable margin in the income of the people to allow them to accumulate these huge

* The Indian Fiscal Commission had to consider this problem. The minority report is anxious to raise some safeguards against the deleterious influence of the foreign capitalist. Such measures have failed in Germany and they are bound to fail in our country also. The only safest course is the accumulation of our capital and our capitalists should become the natural heirs of foreign enterprise in our country.

hoards. It is undoubtedly true that small sums are saved but these can never be styled fabulous hoards. The frequent occurrence of famines dissipates these small amounts into thin air and it is really as a sort of protection against these famines and pestilences, that these people do lay by something.

Another fact which demolishes the theory of hoards is the appalling indebtedness of our peasantry which has been estimated by the late Mr. G. K. Gokhale at £250 millions. Such a vast amount of rural indebtedness and its chronic universality can hardly be squared with the theory of huge hoards.*

The chief reason responsible for this unwise habit is the illiteracy of the population. In the past there was nothing but invasion, misrule and brigandage and the habit of secret accumulation due to the insecurity born of these troubled times has still to be eradicated. The wealth of the zamindars and the richer professional classes is being utilised for industrial purposes to a certain extent. There is a considerable accumulation of precious metals in the shape of ornaments. As Sir D. M. Dalal says "money lies dormant in endless small hoards." It is a well-known fact that some of the agriculturists and middlemen have made profits during the war time. Owing to the lack of banking facilities for

* In Punjab the interest paid by cultivators annually to the money lenders is double the land revenue. Dr. Gilbert Slater in his "Some South Indian Villages" says the same thing about the Madras Agriculturists. Dr. H. Mann's recent estimate about the indebtedness of the Deccan ryot is to the same effect. These annual drains for interest leave little for accumulation.

the people these prefer to hang their savings in the shape of investment in jewellery. Every man considers his wife as his banker and so long as this is the general tendency the banking habit cannot be created.

The agriculturists and mofussil traders should be taught that a bank affords the best store of value relieving them of the risk and trouble of keeping large stock of precious metals in their house. The advantages of a banking account have to be inculcated into their minds. Even those who are aware of these advantages do not come forward frequently to the bank to carry on their transactions. These have no confidence in the financial stability of the banking institutions and when once they have witnessed these mushroom banks disappearing as fast as they have sprung up they are reluctant to trust them.

Thus capital in the mofussil is totally unorganised and the transfer of money is purely a personal transaction between the payer and the recipient. In Europe branches of banks are established in small places and the branch bank is made to open its office once or twice a week in order to transact business. But such is not the case with the Indian banks.

Again the habit of hoarding is said to have been revived at the outbreak of the war. The alternately swaying fortunes of the belligerents on the battlefield have only confirmed the sad tendency on the part of the people. To add to this the official restrictions impeding the free importation of precious metals on behalf of private people into our country have had something to do with this and in fact have

gone a great way to encourage the people to hoard their slender stock of precious metals. The wealthy people prefer investments which pay much more than the banks can hope to pay. Investments in land by purchase or mortgage still appeal to the majority of the people who can afford them and the investment of money in Government paper exercises a strange fascination on the minds of various classes of people. As yet the banking habit has not been deeply implanted and until the people realise the importance of this habit the day of our economic salvation is far off.

Just as the principle of thrift is inculcated to school children so as to make them thrifty so also should the principles of a banking account and the way of opening an account and subsequent dealings with the bank might with advantage be taught on the impressionable minds of school children so that they might profit themselves in their mature age. Again it should be a systematic policy on the part of the educational authorities to teach the elementary principles of business, financial and economic subjects in the secondary schools and much time should be devoted to the familiarising of these youths with the methods of banking and the acquainting of them with the advantages of a banking account. As Mr. Vidyasagar Pandya suggests "small penny banks may be attached to certain schools as in England" to encourage practical thrift.

Many of the English Joint Stock Banks issue small touting circulars explaining to the people what foreign exchange is and how it is conducted by it,

A similar device should be adopted in a backward country like India. Vernacular circulars can be issued by each bank stating the principles of banking, the advantages of a banking account and the bank's own progress from year to year. These will convince them as to the utility of the banks. In England it has been said that every man has his own solicitor and his own bank. Although our people are rapidly achieving the first part of this ideal much to their own detriment they have not copied the more paying and useful habit, namely each person having his own bank.

3. *A Branch Bank System.*

The Report on the Moral and Material Progress of India* says "there are at present in all India under hundred head offices of the banks with 322 branches. The proportion of the total towns in India with a population of ten thousand and over in which banks and their branches are situated is still only 25 per cent." The following table gives an idea of the banking institutions of the following countries.

	India.	United Kingdom.	U. S. A.	Canada.	Australia.	Japan
Number of Banks	87	54	31,000	18	16	2052
Branches	380	9,547	,,	4,865	2,995	4,589†

The Marwari banker and other indigenous confreres of his carry on a lot of banking business but no statistical information can be obtained as to

* India in 1921-22, edited by L. F. Rushbrook Williams.

† This table has been compiled from the returns furnished by the official year books. The table relates to the official year 1920-21.

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the number of their agencies and branches. Making due allowance for these one does not find that branch banking has progressed very favourably in India.

It has been estimated that no less than 9,547 banking offices exist in the United Kingdom and although India is nearly 15 times greater in area and seven times larger in the matter of population than the United Kingdom one notes that it is seriously underequipped in respect of her banking institutions. In Scotland it has been said that "every village has its own bank" and Mr. MacLeod says "what Nile is to Egypt so is the banking system to Scotland, a fertiliser." Happy would be the day when each big Indian village would be in a position to boast of its own humble banking office. At present many a town* with a population of 20-40 thousand inhabitants goes without even a branch bank whereas it has been remarked that in England "every town with a population of 20 thousand people has been overbanked." In many places the starting of a branch bank is viewed with apprehension and every attempt to tout for business is deprecated.

Unfortunately the case is not so with India. In the first place there are not many sound banks conducting business on sound and conservative lines—the Imperial Bank and the exchange banks excepted. The rest of the banks with the notable

* The Government of India looks forward to the establishment of a branch of the Imperial Bank in every district and every town of importance. Roughly speaking there is at present one banking office for every 900,000 persons in India.

exception of the Allahabad Bank are new-born institutions and the crisis of 1913-15 has weeded away the speculative and the less stable of the Indian Joint Stock Banks. The rest of the banks are labouring under the difficult and slow process of building up their business but it is apparent that the existing number of banking offices are totally inadequate to meet our growing needs. As the Indian Industrial Commission says "the banking facilities are surely non-existent to the major part of our population."

Every economically advanced country has accepted the policy of branch banking as the safest possible means of expanding the utility of their progressive banks. Alexander Hamilton has been credited with the honour of being the originator of this branch banking system. Canada took it up. Both in Australia and Japan there is a highly developed system of branch banking. It has become a settled fact and one finds it thoroughly established in the United Kingdom and the continental countries.* But for the fact that the national banking law of U. S. A.† has prohibited branch banking and that the various state laws do not encourage it, it would

* The German bank policy is very progressive in the matter of branch banking. In addition to their head office they have "Filiales" or branches. They have also "Commanditen" that is silent partnership in private banking houses supplying them with capital. They have also "depositen Kassen" or deposit offices in all German towns. Originally intended as deposit branches they have now become complete banking institutions by themselves helping parent banks to bring an increasing circle of clientele and help their issuing power. It also extends the cheque, giro and clearing business of the present bank. *Vide* Dr. Reisser—"The German Gross Banken."

† *Vide* R. P. Eckhardt, The Rational Banking System.

surely have spread itself there also. With the passing of the Federal Reserve Act of 1913 a change has come over the situation and the National City Bank of New York is organising its foreign branches systematically. Even the Federal Reserve Banks are now allowed to have branches in their districts. The evolutional development of international banking and the branch system gradually dispenses with the services of the intermediaries and leads to greater and all-round financial strength, efficiency and responsibility.

India ought to learn and profit by examples set by other countries. All the sound banks doing business on conservative lines should be made to extend their branches into the interior and establish a network of banking establishments, to serve as connecting links between the various parts of the country. The starting of new banks is a difficult affair and whatever might be said in favour of independent local banks, the verdict of experience specially in the United Kingdom and Canada has gone against it and the branch bank system has come into vogue.

The opening of branches will afford an outlet for the surplus capital at the head office and minimise the danger of its being invested in hazardous undertakings. They afford facilities for the transmission of money from one place to another, and can easily bring about a distribution of capital according to the relative needs of time and space. The small traders might be educated as to the advantages of a banking account. The branches will afford the best possible professional training ground for young people

desirous of a new career. Expenses of management can be economised. The opening of branches all over the country would lead to a lowering and steadying of the rate of interest to a great extent. It will lead to an increase of loanable funds.* The various branches will give ample facilities for gaining information of the state of customers and also of the nature of their work. The branch bank system may be extended to places too small to support a regular bank which requires a full complement of officers and reserve of coin.

But there are some disadvantages of the branch bank system. Each branch is a source of weakness and loss at one branch may lead to a run on the whole establishment of which the branch is only a part. The branches may tend to rival the older establishments of the place (if any) and this rivalry may lead to the lowering of the banking standard. There may be a falling off in the nature of securities against which banking accommodation is sought and over-branching may lead to over-banking and the extreme rigour of modern competition will force the numerous branches to tout for unsafe and risky business. An undue and disproportionate multiplicity of banks will be co-existent with a tendency to indifferent banking finance. Too many branches and all of them working under rule of thumb methods will tend

* "The deposit habit," as Bagehot says, is a very difficult thing to begin because people do not like to let money out of their sight without security still more, cannot all at once agree on any single person to whom they are content to trust it unseen and unsecure. But a branch of big city bank conducting business in their midst effectively dispels this suspicion from their mnids."

to stifle intelligence and the branch bank system might tend to remove superfluous capital from the provinces into the metropolis and thus the provinces might view the draining away of money with disfavour.

Many of the above-mentioned disadvantages are not inherent in the branch bank system nor are they the inevitable concomitants of it. Most of them can be eliminated by instituting a system of effective audit and insisting upon weekly reports of business from the heads of branches to the head office. There should be a clever training imparted to these officers at the head office before they are sent out as heads of branches. An efficient peripatetic supervision * by the manager of the head office would obviate many of the above defects. Some of the directors should make unexpected visits at the branch offices to see the way the business is conducted. The branch banks if established in response to actual demand, if they follow strictly the legitimate duty of attracting deposits, if they keep down expenses to a proper level, if they confine themselves to mastering the credits of their customers and if they eschew all rivalry with the existing older banks and be amicable with new rivals that may enter the field there is no reason why they should fail and cause ruin to the parent bank. Local business men may be appointed to advise the branch managers as to the granting of loans and to study the needs of particular

* There should be a chief inspector for each large bank and these inspectors must issue confidential reports as to the state of banking business conducted by the branches.

localities and gauge the personal credit of the customers of the bank. Reasonable allowance of power and discretion of action should be allowed to branch managers who may be induced to identify themselves with the people of the locality by their activities and pursuits. If these injunctions are strictly observed by the branch managers the branch bank system affords the best solution of increasing banking facilities in any particular country.

Although the salvation of India lies in this particular direction several well-informed people consider that a rapid increase of branches can never take place as there is a pitiable dearth of trained banking employees available to work these branches satisfactorily. Some are of opinion that it is of no use to merely increase the number of branches so long as the present psychology of bank depositors continues unchanged. The first breath of ill wind scares away the Indian depositor and a convincing testimony occurred so recently as in the case of the failure of the Alliance Bank of Simla.* Sir Bernard Hunter says "the Indian customers go in to the branches only for loaning purposes. The inflow of money is not very substantial so the branches act as an outlet for the remunerative employment of the parent banks, loanable resources and not as feeders to the slender reservoirs of their parent banks. The question of expense has also to be reckoned. A new branch takes some time to pay its way. The

* In 1924 March there was a similar run on the Bhawanipur Banking Corporation.

Imperial Bank should not murmur on this score because the expense would be quite insignificant when compared with the profits they can make with the Government deposits.

Coming to actual practice one finds that this branch bank tendency has taken root in this country.* Owing to the present depression of trade, the mammoth expansion of the Imperial Bank and the recent bank failures the managers of the indigenous banks are diffident as regards the policy of branch expansion. No doubt these conditions will soon pass away but the lack of trained banking employees to work the several branches is a real obstacle in the path of extension. This absence of trained bank officers has been due to two reasons. It is only the European that has taken up the banking business as his avocation and few qualified Indians aspire to have a successful banking career. The unsympathetic attitude of the managers of the immigrant banks is partly responsible for this state of affairs. While the

	Name of the Bank.	Branches
1.	The Central Bank of India ...	16
2.	The Punjab National Bank ...	25
3.	The Bharat National Bank ...	6
4.	The Poona Bank	6
5.	The Bank of Northern India...	5
6.	The Indian Bank... ...	4

The People's Bank of Lahore had 80 branches. The Alliance Bank of Simla had 51; The Tata Industrial Bank, 26; The Industrial and Exchange Bank of Bombay, 40. The first two banks have failed. The third has amalgamated with the Central bank. The fourth has recently suspended payment (March 10 1924).

European officers are shifted from department to department to grasp their routine the Indian officer has to literally rot in one department before he can have the opportunity to master the work of another department. This unconscious stifling of all chances and narrowing the scope of his vision have only tended to deaden his faculties.

As regards the psychological objection it must be remembered that financial confidence is a plant of very slow growth and needs careful nurturing. It is barely a few years since our Indian Banks managed by Indian officers have been conducting business. Mutual confidence between the bankers and the public is only a question of mutual sympathy and general prosperity.

Coming to the argument of Sir Bernard Hunter it must be noticed that it is not an objection to the starting of branches. Only he advises caution on the part of bankers who may be anxious to increase their branches out of all proportion to the loanable capacity of the banks. When requested by Sir David Yule to reorganise the Alliance Bank of Simla* his first advice was to close some of the branches which were not earning any amount of profit. Any dissipation of the Bank's reserve in several places would tend to increase the vulnerable parts in its armour. It is this that must have prompted Sir B. Hunter and other founders of the Imperial Bank to refuse to accede to the wishes of Rai Saheb Seth

* *Vide* Sir David Yule's speech to the shareholders of the Alliance Bank of Simla at their annual meeting held in August, 1922.

Nathmal.* As a banker's bank its position must be impregnable.

But the remarkable pity of the present situation is that branches are not established in places which do not possess banking facilities but only in district capitals, populous towns and the chief monetary centres where banks already exist. Banking facilities should be extended to the interior of the country. The small agriculturist, the petty artisans and the local traders are those who are the chief sufferers and our banks should by extending their deposit, discount and loaning functions spread a useful fringe of benefits over the entire community and protect it from the money-lending Shylocks.

But a far greater number than the existing branches are required. In short the crux of the situation lies in the attracting of more capital to the vaults of the banks. This should be done by increasing the authorised capital after getting the necessary legal permission. Our old and well-tried banks which have borne the scrutinising tests of time, and have come out purified and strengthened by the ordeals of several crises should extend their branches. It would be extremely unwise and dangerous to entrust our deposits to new banks whose integrity has not been proved, whose stability has not been put to the test and whose solidity is still a matter of question. These will be subject to all the ills of infant

* Rai Bahadur Seth Nathmal wanted the Imperial Bank to establish its hundred branches in places which do not possess any banking facilities.

banking and India can ill afford to lose the little capital she possesses. The next phase of development in our banking business would be the financing of our country by means of a well devised system of branches strategically situated so as to tap the deposits of the people and minister to their economic needs wisely and beneficially.

While in Western countries attention has been drawn to the branch bank *versus* the independent local bank controversy, in India on the other hand some ignorant persons might find an apparent conflict of interest between the branch bank expansion policy and the development of urban co-operative banks. Mr. H. Dupernex and Professor J. C. Coyajee have been the staunchest exponents of the urban banks extension policy. Both of them realise that the joint stock banks are handicapped as their foreign managers find it difficult to expand their branches and gauge the personal credit of local customers. Hence urban banks should be started to mobilise the unorganised capital in the interior and to provide financial facilities for the small industrialists and the artisans and familiarise the people with forms of credit as notes and cheques and give them sound currency education in the matter of paper currency circulation.

But the chief difficulties hindering the growth of the urban banks are the want of leadership, lack of co-operative spirit, the spirit of commercialism, lack of capable management and a " wide difference in the moral outlook of the town people." Hence

urban banks have not increased to such an extent as the agricultural credit societies though both have been started at the same time. It is only in Bombay, Ahmednagar, Poona, Belgaum, Dharwar, Calcutta, Chittagong, Mymensingh, Pabna, Jalpaiguri, Madras, Chengalpet, South Canara, and Salem that one really comes across progressive urban banks. As the bonds and basis for co-operative union are so very many in our society even this little success is possible. The great sociological factor, caste has been contributing to their success, moreover the failure of these swadeshi banks has given a decided impetus to their growth. Employees' societies have also been flourishing mainly due to the privilege of deducting loans at the source out of salary.

But much more real work can be done by utilising the machinery of committee management as in Italy and employing banking officers or trained members of the Indian co-operative service as secretaries of these urban banks. It is only by these urban banks or by a development of the branch bank system that banking facilities can be organised. Till then "the Indian people will be minus all that makes the wheel of life turn smoothly—minus water, food, clothes, oil, sanitation, doctors, medicine and education. These are chiefly traceable to money that vacuum in the body politic—the banking system for which India so wearily waits."*

* *Vide* Sir Daniel Hamilton, Policy of Development, in the Indian Co-operative Studies—Page 255.

4. *The training of Bank Employees.*

Another noticeable feature is the lack of trained banking managers possessing complete knowledge of banking theory and an adequate amount of practical experience. The Indian Industrial Commission observes "that there is a lack of trained bank employees owing to the absence in the past of facilities for commercial education and of any regular system of training Indians in banking work while the countryfolk are not alive as to the advantages of organised banking." The Lahore Committee says that there is a strong need of promoting a knowledge of banking systems among the people and it emphasises the necessity of training people in banking work. Pandit Madan Mohan Malavaiya says "the Government of India should take definite steps to impart the best instruction to young Indians in banking through the best teachers it can appoint." According to him one of the advantages of a State Bank should be the providing of facilities for training Indians in banking work.

Pandit Malavaiya instances the marvellous development of banking in Japan as due to the training of its people in the banking business. "At the time of Restoration in 1868 there was complete ignorance of the methods of finance or of banking or of joint stock companies. National economy and finance were both in perilous condition." To remedy this Prince Ito was sent to America to study the working of their financial institutions. On his recommendation national banks were organised and the Imperial

Bank of Japan was next established as a Central Bank. At the present time separate banking institutions deal with the different kinds of banking business. Baron Shibusawa says the same thing.*

The prime requisite for possessing a good banking system is to have a number of persons who have had a grounding in the theory of banking with a fair amount of practical knowledge in some of the different banking systems of the foreign countries. As Mr. Shirras says "Just as trained teachers are of first importance to Indian education at the present time so are trained officers in sufficient numbers to Indian banking.† At another place he says "Without trained leaders the banking army will never win a victory and we shall have to depend almost entirely on that hard working body of men who bring to the East the banking wisdom of the West." He recommends that our Universities and the colleges working in greater co-operation with

* "Before concluding this essay the writer cannot refrain from expressing his profound satisfaction at the fact that the small spring of banking business which had been so insignificant at the time of the Restoration has by a gradual process of accretion became a broad and navigable river as it is now and his conviction is that this is the result of having followed the example of European and American Nations. The Japanese are very grateful for the valuable services of Mr. A. A. Shand now a director of the Paris Bank, London, who came to Japan at the invitation of the Issue department in 1872, acted as the adviser in banking to that department, wrote valuable books on banking, instructed young Japanese in that line and thus paved the way for the development of banking business in that country."—Count Okuma—" Fifty years of New Japan."—Vol. I, p. 352.

† Mr. G. F. Shirras—Indian Finance and Banking—page 432.

banks should do more than they have done in the past."*

Even in the United Kingdom the heads of the great banking establishments are not satisfied with the quality of men that is being attracted to the bank offices. Although there is a banking career existing there attempts are constantly made to attract the best possible men to the banking business. As Walter Leaf says "The banking career must be placed in a light as to be on a par with the most lucrative professions existing now."†

The late Lord Faber, the President of the Country Bankers Association said that "the banking career should be placed on a footing by which it will compare favourably with any of the learned or professional careers in the country." He suggested that "youths already in banking service should be given scholarships to enable them to take a full three years' university course in commerce as a part of their career."‡

In future increasing attention has to be paid by the Indian banks while recruiting their Indian element in the banking staff. It should be remembered that "the English Banker in India is not always all that can be desired of a banker. He is lacking as much as the Indian banker in that superior

* Ibid—page 420.

† Walter Leaf's Presidential Speech at the Annual Meeting of the Parr's Bank, 1919.

‡ Also refer to Lord Faber's Presidential Speech at the Annual Dinner of the Institute of Bankers—January to June, No. 1919, Journal of the Institute of Bankers. Therein he relates how American banks recruit their clerical force from the public Schools of New York.

realisation of the nature and object of banking. "It is an open secret in the money market that sometimes X the manager of the bank A speculates in the name of his personal assistant in the shares of the company and how Y the secretary of the bank B gambles in cotton. That neither X or Y is easily found out speaks indeed highly for the perfection of his education in so conducting its operations as to leave hardly any evidence that could be accepted in a court of law. Such sort of men cannot be the requisite morals for our Indian officers to copy."*

As we find that even the European banker is not the ideal banker we should lose no time in preparing and training men of our own country. The sooner we rectify this defect the easier will be the task of obtaining for India a financial ascendancy to which she is entitled by virtue of her natural resources and great financial strength.

The formation of debating societies, the equipment of an up-to-date library in banking offices, the granting of scholarships to proceed to Europe and America to learn the ways of commercial banks and the transacting of foreign exchange business and the contribution of articles by senior officers of banks in banking journals to give the benefit of their experience to the junior officers are some of the measures which have to be undertaken by the banks to improve the knowledge of their staff. It is false economy to rely on an incompetent staff.

* *Vide* Tannan and Shah "Indian Banking and Currency Problems"—page 241.

5. *A Bankers' Association.*

The friendly intimacy and comradeship engendered by the presence of several banks in the Bankers' Clearing House has borne fruit in the various associations that have been started in all countries, where banking progress has reached an advanced stage: The credit of starting the first Institute of Bankers belongs to Scotland. It was started in 1875 and to-day its members number about two thousand six hundred. The Institute of Bankers in England was started in 1879 and it has now a membership of 15,083. The Institute of Bankers in Ireland was started in 1898 and it has on its roll about 800 members. These institutes consist of the officials of the banks in the country. Strong bankers institutes have been started in Canada, Australia and South Africa on the model of the English Institutes. These institutes have carried further the idea of the bankers' associations which aim at providing a common platform and meeting place for the various banks to assemble and discuss their common topics. In Germany there is a "central federation of banks and bankers" to discuss banking topics. In America there is every year "The Annual Convention of the American Bankers' Association" and all interesting developments and new departures in banking methods are keenly discussed.

Other Aims.

The suitability of rates charged by the various banks and their co-operative adjustment so as to

eliminate competition and rivalry is one of the chief objects of these associations. Measures for banking reform and legislative proposals affecting the banks as well as their suitability or non-suitability to domestic conditions are fully discussed. A knowledge of the science and art of banking is imparted to the banking officials by means of lectures, classes, libraries and reading rooms provided by these associations. Well-conducted magazines discussing foreign banking methods and improved innovations are the usual official organs of these bodies.

The Example of Canada.

The Canadian Bankers' Association goes a step further and performs the following functions in addition to the work of propagating sound banking methods and instilling the ideas of common fraternity in the minds of the bank officials. It looks after the note circulation of the various banks. It holds periodical examinations, by means of its inspectors, of the bank's position as regards its note circulation and reserve. It undertakes the work of liquidating all failed banks, and the Canadian Banking Law compels every recognised bank to become a member of the association.

Results Achieved.

The idea of fraternal relationship which has been developed by the bankers' association has permeated the minds of bank officials in England who

have formed themselves into a guild. It consists of all bank clerks and its object is to protect the interests of its members and to improve the knowledge of the junior members. To establish closer contact between the superior officers and the younger members of the staff is another useful object of these guilds. Banking has been recognised as a distinct profession with its own policies and traditions. The wider interests and responsibilities of the bank are clearly grasped so that the old narrow profit-making motive is slowly yielding to the higher ideals of national development and material progress of the community as a whole. Banks are well conducted and a spirit of noble emulation actuates all the leading concerns. National credit is guarded carefully and as a result of the better understanding of the true principles of credit, currency and capital serious panics have become an occurrence of the past. Crises still occur but the rude shocks of sudden panic are prevented by the excellent management of the banks. This is solely due to the class consciousness created by the Bankers' Association, and the better understanding of the principles of banking profession which is only an indirect result of the educational propaganda of these associations.

One Such Association Needed.

If such are the manifold advantages that can be realised from the successful functioning of a really progressive bankers' association no time should be lost in starting such an association in this country.

The Eastern Exchange Banks have an association of their own wherein are represented some Indian Joint Stock Banks conducting foreign exchange business. The indigenous bankers have their own associations but there is no common platform or meeting ground for all bankers, the old and the new, the immigrant and the Swadeshi, the expert and the amateur, to come into contact with one another. As the Lahore Committee says "there is no association of bankers to look after the general policy of banking development as a whole."

Suggestions.

It is highly imperative that a bankers' association should be formed including all the prominent officials of all the big banks. It should meet once in four months at least so that it may afford scope for the free interchange of knowledge on matters that concern them all and such procedure will not fail to benefit all the banks individually and Indian Banking as a whole.

This association should undertake the dissemination of sound ideas, the suggestions of useful reforms and the spread of profitable knowledge and should serve as an educational force at work among the bank employees. It should undertake to organise a course of lectures corresponding to the "Gilbert lectures" of the Bankers' Institute of London to tackle with problems of Indian banking and arrange for the delivery of useful lectures to enable bank clerks to grasp the theory and practice of bank-

ing. It should have a monthly or quarterly magazine of its own entitled the Indian Bankers' Magazine where all recent improvements of foreign banking methods and their applicability to Indian conditions should be discussed. This would be best practicable measure that can be undertaken at present to improve the wisdom and knowledge of our bank officials. It should undertake the collection of banking statistics that may be of use to any future economist and historian and a periodical publication of balance sheets. The creation of a bankers association would undoubtedly lead to a unity of policy, the prevalence of common sentiment among the several banks and would bring about an *entente cordiale* between the Indian managed and the European managed banks.

6. *The Development of the Existing Clearing House System.*

The clearing house system that exists in India* does business on the model of the English clearing house system. It has not copied the model of the

* There are about seven clearing houses in the following places :—**Calcutta, Karachi, Bombay, Madras, Rangoon, Cawnpore, and Lahore.** The Imperial Bank facilitates the clearing business in all these places. **Calcutta has 23 banks,** Bombay 32, Madras 8, Karachi 11, Rangoon 10, Cawnpore 9, and Lahore 13. More clearing houses should be started in Amritsar, Delhi, Lyallpur, Lucknow, Rawalpindi and Allahabad. Amritsar has 9 banks, Delhi 11, Lyallpur 9, Rawalpindi 7, Allahabad 7, and Lucknow 8 banks. The Imperial Bank has a branch operating in these centres. It should take the lead and start the C. H. Organisation. The private banking firms should join the Clearing House Organisation in order to increase their utility.

American clearing house. The English clearing house may be defined as a device to simplify and facilitate the daily exchanges of items and settlement of balances among the banks. The clearing house in America not only performs these functions and secures the well-known economies of time, labour and money but it goes further and acts as a medium for united action upon all questions affecting the mutual welfare of the banks.

In America some of the following functions are performed by the clearing houses.* They take up the question of extending loans to government. They fix the minimum rates of interest which the banks pay to their depositors. They fix uniform rates of exchange and charges of collections. They hold an independent system of bank examinations. They issue clearing house loan certificates to the banks doing sound business on good assets and on the strength of these certificates these banks can borrow. It was by means of this device that the American National Banking system tried to remedy the defects arising out of the absence of a Central Bank. As Mr. R. G. Hawtrey puts it "this process was a rudimentary analogue of the rediscounting facilities given by the great European Central Banks. It was an expedient born of sheer necessity and was itself an evidence of the urgent need for reform."† The Federal Reserve Act has

* *Vide* J. G. Cannon, "Clearing Houses."
† R. G. Hawtrey—Monetary Reconstruction, page 94.

introduced a system of rediscounting as in the case of the European Central Banks.

On the European Continent the Clearing House system has recently been started and it does not play such an important part because all the countries possess a centralised banking system. The central banks do a large business in current accounts and the transfer and remittance of funds are accomplished largely by cancellations through book entry.

Unfortunately for us we have neither a responsible Central Bank nor an efficient, enterprising and go-ahead clearing house system as they have in America. If the Imperial Bank is able to throw open rediscount facilities to all the important banks, the privilege of being on the rediscount list would be almost as much coveted as the privilege of being a member of the Clearing House. The Imperial Bank should scrutinise the position of all the members on the rediscount list now and again and weed out all unsound concerns from its list. This itself acts as a most salutary check forcing the ordinary banks to conduct their discount business on scrupulously clean lines and helps to improve the banking standard.

Such an extension of privileges would lead to closer co-operation between the Indian joint stock banks and the Imperial Bank. It is only by an extension of this privilege can the Imperial Bank extend accommodation to the growing needs of traders in India. A trader's bill bearing only one signature is never discounted by the Central Banks.

The same is the case with the Imperial Bank. Hence there should be an intermediary to enable the trader to obtain the needed accommodation. There would be no greater and more secure intermediary than a joint stock bank and it is only through these banks that accommodation will reach the mass of traders.

Another grave reason why the rediscounting of bills should be an important feature in the case of our Indian banks is that these do not generally possess ample financial resources. They do not attract much of deposit money hence there is no reason why the banks should be hindered from supplementing treir resources by having access to the Central Bank.* It should be a legitimate branch of their business and so long as these banks do not maintain a ridiculously small reserve simply because they can augment their capital by rediscounting the bills easily, there is nothing opposed to sound principles. Rediscounting is the only safest and cheapest method of placing credit facilities in the hands of the smaller banks. Without the power of issuing notes the Imperial Bank cannot however undertake to supply the other banks with the needed amount of capital.

* In the Continental Countries the smaller banks have access to the Central Banks by this rediscounting process and they are able to do much service to the trade and industry of their countries. In England this rediscounting of bills by the smaller banks is not liked by their customers who object to their paper being "peddled" about.

7. *The Co-operation of Banking and Note-Issuing Function.*

Another noticeable feature of our banking system is the divorce of note-issuing from the banking function. It is true that in many countries the banks of deposit do not issue notes. But the central bank is both a bank of deposit and a bank of issue. Thus all banks of issue happen to be banks of deposit.

Before the year 1861 when the Government of India took the note issue into its own hands all banks had the privilege of circulating notes as a free banking system prevailed at that time. But the notes of the Presidency Banks enjoyed a higher status than the notes of other banks in that they were received by the Government to some extent in payment of revenue.* Still the Presidency Banks failed to circulate a considerable amount of notes. This restricted circulation was solely due to the fact that these notes were not legal tender. The public had no faith in the financial stability of these institutions. The first banking crisis of the years 1829-32 swept away many of the banking houses. Naturally the people were chary in reposing confidence in the surviving institutions. Again the habit of the people was to circulate metallic coins and they had a passionate liking for the metallic ringing of

* *Vide* F. C. Harrison, Economic Journal, 1891, Vol. I, p. 726.

these coins and hence the notes could make no headway against the current of popular disfavour. Besides these difficulties, the banks were hedged in by legal restrictions,* *i.e.*, notes could not be issued beyond an amount which is four times its cash reserve. Labouring under these difficulties their early note circulation was not an appreciable one and the notes failed to win popularity as a medium of exchange.

The Hon'ble Mr. James Wilson who was brought out to India to reorganise the finances of the East India Company which fell into disorder on account of the great Sepoy Mutiny of 1857, recognised these difficulties and at once planned a scheme for the substitution of Government notes in place of the bank notes. The year 1861 inaugurated the new era of Government Paper Currency, but a serious mistake was committed in accepting the 1844 Bank Charter Act of England

* These restrictions were not extended to other banks issuing notes as their notes were not so privileged as those of the Presidency Banks. Another reason why the Presidency Banks were subject to these restrictions is to be found in their close relationship with the government. *Vide* Appendix I of this book which gives a brief account of the Presidency Banks.

† Although the Act XXIV of 1861 organised government paper currency the Presidency Banks were employed to superintend, manage, and become agents for the issue, payment and exchange of promissory notes of the Government of India and for carrying on the business of an agency of issue on a remuneration of ⅜ per cent. per annum on the daily average amount of government currency notes outstanding and in circulation through the agency of the banks. The Secretary of State disliked this arrangement as it seriously compromised the principle of complete separation between the business of issue and banking business. See the House of Commons Returns—East Indian (Paper Money) 215 of 1862.

as the only sound principle of regulating the note issue and this was done in spite of the vehement protest of the worthy originator of the scheme. From 1861-1866 the Presidency Banks issued the paper currency through their channels of business but ultimately it was handed over to the Paper Currency department. But from 1861, all banks have become mere " banks of deposit."

In England all the banks existing prior to 1844 were given the right of issuing notes up to a certain limit; but as a matter of practice these banks do not make full use of this privilege and the Bank of England is given the sole right of note issue in England and the Issuing Department has been separated from the Banking Department and similar results have been reaped in both cases. The currency system was rendered inelastic and whenever more currency is required in times of moving the crops or during the abnormal times of a crisis the currency pinch is acutely felt. The Bank of England supplies emergency currency by expanding its book entries for other banks and those which treat "cash in the Bank of England as equivalent to the cash reserve" as soon as their cash at the Bank of England increases, supply the needed accommodation, but during abnormal times the suspension of the 1844 Bank Charter Act has been unavoidable. It would have been removed out of the Statute Book long ago, had not the English nation hit upon the admirable cheque system which has bestowed the needed elasticity to their currency system.

Unfortunately for India, the inelasticity of her currency system has become a permanent feature and no such palliative as an efficient cheque currency has become popular. Till 1920 the Independent Treasury System used to aggravate the whole situation and the government intensified the stringency by always "maintaining a policy of traditional aloofness from the money market."* All these causes have intensified the need for securing elasticity during the busy season and various remedies have been proposed. The issuing of inconvertible notes during the busy season, the giving out of loans from the government balances of the paper currency reserve, the privilege of access to the London money market to enable the Imperial Bank to obtain more funds and the increase of the working capital of the banks have been severally proposed but these are mere palliatives and not permanent and efficacious remedies.

The Reserve Treasuries have been amalgamated with the Imperial Bank and access to the London money market has been granted. More paid-up capital has been insisted upon and it is confidently hoped that the problem of shortage of trade capital would be solved. But it must be borne in mind that the trade requirements of India are growing every year and the funds of the government Reserve Treasuries are too slender to meet the actual trade requirements

* Sir William Meyer however pursued a more intelligent policy in placing all the balances of the Government in the hands of the Presidency Banks.

of India. Access to the London money market would in pre-war circumstances have been an effective solution but now the wastages of war have to be repaired and the little capital that will be available will go to the stabilising of the Industrial machine whose gear has gone out of order. The London money market can ill spare her funds to meet the requirements of the Indian money market. Owing to the disturbed political conditions and the frequency of labour disputes the foreign capitalists would be apprehensive of the future and even though discriminating protection may be adopted yet the flow of capital is bound to be rather weak in the future. There are many other factors hindering the potential mobility of capital and these lie outside the scope of the banker.* So dependence on outside factors should be out of the question and so long as the American exchanges are against Great Britain their first attempts would be diverted to home production and the export of raw material so as to correct the unfavourable turn of exchange. It is hopeless under these circumstances to expect any relief from this source. The above three methods might act as mere lubricants in the present situation but they are not permanent and radical remedies for the chronic shortage of trade capital.

* Of late Indian industrialists tried to coax foreign capitalists into Indian enterprises but they have refused to undertake local risks and have only subscribed for a safe proportion of debentures. Even well-established Indian enterprises are finding it increasingly difficult to attract foreign capitalists so easily as before.

The first thing required is that the banking function should be co-ordinated with the note-issuing function just as one finds in France. It should be entrusted to the Imperial Bank. The days of decentralised note-issuing have passed away and the Imperial Bank should issue the notes under regulations laid down by the legislature. Until the Imperial Bank has full power to expand its note issue in response to trade requirements the problem of shortage of trade capital will not be successfully solved.

But in the meantime the needed elasticity of our currency system should be furnished by some device or other. The seasonal expansion of twelve crores of rupees on the strength of export bills as laid down by the P. C. Amendment Act of 1923, does not suffice.* The government should realise that "the present stringency is due to the conversion of international money that India gets for its exports" and according to Hon'ble P. Sethna the "sale of council bills on account of the paper currency reserve should be sold at a fixed limit never lower than one

* Sir Purushotamdas Thakurdas recommended 20 crores to be fixed as the maximum limit of this emergency currency. Mr. P. Sethna, Chairman of the Board of Directors, the Central Bank of India, recommends the issue of five per cent. of outstanding paper currency notes as soon as the bank rate is six per cent. and three per cent. to be issued as the rate rises to seven per cent. and two per cent. as the rate rises to eight per cent. But this method would not yield more than 17½ crores and probably these limits might not be sufficient to enable the Imperial Bank to successfully loan its balances during the busy season as its proportion of cash against liabilities may begin to decline seriously.

shilling four pence.''* This is a tentative measure for the time being.

The state issuing of notes has led to their popularity and wide acceptance and the public might dislike the transfer of the note issue. They should realise that the note issuing function is a part and parcel of the banking function and it ought to be entrusted to the Imperial Bank which should be responsible to the government for its sound and successful management.†

All authors of the numerous proposals of a State-Bank unanimously agree on this point. It is only through the agency of the banks that a note circulation can ever attain of the banks that a lopment throughout our country. Again it is through the agency of a bank that a note issue can be made flexible and responsive to the needs of the community. The Imperial Bank should be utilised to educate the people in the use of paper currency.‡

The real remedy is the tapping of more capital from the pockets of the people. The 'banking

* *Vide* Mr. Sethna's Speech, Annual meeting of the shareholders of the Central Bank of India, March, 1924

† To enable the Imperial Bank to have its own notes both the P. C. reserve and the G. S reserve should be handed over to it. For allowing this privilege the Imperial Bank should pay a certain rate of interest on the total note circulation in excess of the metallic portion kept as reserve of its notes.

‡ It is preferable to have an increase of paper currency through the hands of the Imperial Bank rather than an increasing use of token currency. As Professor Pierson says "The great increase of token currency. As Professor Pierson says, "The great increase of movement in the domain of currency. Almost the whole of the money should be standard money."

habit' has to be inculcated. The people should be educated in the economical use of gold and silver they possess. As Mr. Ramsay Macdonald says, "Capital that is used for anything except for the specific and economic purposes for which capital ought to be used, for renewing capital, for expanding the effective capital force of the country is being misused." More of India's raw materials should be converted into finished products and not only should her idle hoards (if they exist) be utilised but the hoarding of her talents, her intellects, her economic opportunities and her unlimited resources should be discontinued.

8. *One Reserve System.*

Another noticeable feature is the lack of concentration of reserves. There are two reserves, so to speak, in India. The various banks have their own reserves and the Government maintains its own reserves. It maintains the paper currency reserve in order to ensure the convertibility of its paper currency. It maintains the gold standard reserve in order to support the gold exchange standard system. But as the Chamberlain Commission has suggested, the paramount duty of the Government is to support the exchange at all times and they conserve all their available portions of stock in order to support the exchange. They have bound themselves definitely to maintain the value of the rupee between certain points and prevent possible fluctuations beyond these points. The government has not abandoned

the gold exchange standard system. They wish to stabilise the system and fix a permanent exchange value of the rupee which will have no relation with the gold value of silver.

Thus the government has a set duty to perform and although the banks may be requiring money urgently they would not be in a position to render any great amount of help, for it may jeopardise their own position; besides they will have to perform the various duties that have been mentioned. The placing of the reserve treasuries in the hands of the Imperial Bank has not relieved the monetary stringency to any appreciable extent. The handing over of the note issue would lead to the placing of the Paper Currency Reserve in its hands, but this takes some more time and the gold standard reserve, it has been said, should not be handed over to the State bank or to the Imperial Bank. Mr. J. M. Keynes argues that "the stability of the Gold Exchange standard system would be endangered by such a step, namely, the handing over of the gold standard reserve to a State bank that would be created." He argues that "the G. E. Standard depends on the strength of the reserve and any unwise dissipation of it by the state bank would lead to the ruin of the system itself."

But there is no harm in giving full discretion to the State Bank to use the G. E. Standard Reserve provided the government carefully supervises the work of the said State Bank. Not only will a sound use be made of the G. S. Reserve but there is the other advantage that the composition of the G. S.

Reserve will follow safer and sounder lines than it does now when it is in the hands of the Secretary of State for India. Again official interference with trade would be discontinued but the government would have to perform the important duty of carefully and judiciously supervising the State Bank. Everything depends on careful supervision.

So there is no necessity for the dissipation of our reserves in so many directions and for the efficient discharge of their functions the existing Imperial Bank can safely ve trusted and the amalgamating of the separate reserves—the G. S. reserve and the P. C. reserve—would not be rash or unwise. The handling of such huge sums would be a heavy task but hands would be forthcoming to do this work and "great men will be produced by great times" alone. Only efficient and careful supervision is needed and there is no reason to fear that these funds would be mismanaged.

Unless indeed that day arrives, when all the funds are entrusted into the hands of a responsible person the problem of the shortage of our trade capital will not be successfully solved. It only remains to add that that day is far off and it has taken three quarters of a century roughly to realise the advantages of a Central Bank. Similarly it will take some more years to make this purely private body more or less a *quasi*-public institution like the Bank of England. But the government must not forget its obligation of careful supervision.

They must remember that "the parcellation of the entire reserve among separate self-indepen-

dent units necessitates a wastefully large proportion of reserve for the efficient performance of the several duties or efficient service with the hazard of unexpected exhaustion of reserves and consequent inability to make good the several contracts."

9. *The Development of the Cheque System.*

One more important feature of the banking system in India is that the cheque system is not greatly in vogue. It is true that an increasingly large number of cheques are passing through the Clearing Houses daily as the following table illustrates it.

LAKHS OF RUPEES.*

Year.	Calcutta.	Bombay.	Madras.	Karachi.	Rangoon.	Cawnpore.	Lahore.	TOTAL.
1914-15	26695	15783	1881	1162*	4312	...	...	49833
1915-16	35286	17718	2021	1409	3950	...	...	60394
1916-17	49289	26228	2529	1736	5068	...	...	84850
1917-18	52490	38353	2301	2217	5286	...	...	100647
1918-19	74113	56946	2545	2230	7385	...	...	143219
1919-20	105576	88302	3395	2313	9474	...	...	209060
1920-21	143993	131593	7599	3342	10484	663	...	297654
1921-22	90501	90673	3954	3673	12202	901	586	202490

* The diminution of the Clearing House figures in 1921-22 is solely due to the stopping of the sale of gold and reserve councils which took place in 1920-21. In addition to these reasons there has been great slackness of trade and decreased activity in share transactions.

The educated classes are slowly acquiring the habit of drawing cheques for large payments.* But as in England cheques should be drawn for small amounts. The habit of drawing cheques is deeply ingrained in them.†

Our people should realise the advantages of cheque currency, the cheapness, the ease and economy that arise out of its increasing use. A well controlled cheque currency is the most elastic thing of its kind. A well adapted cheque system dispenses with the use of currency which might thus become available for the purpose of credit. The development of the cheque currency renders the metallic currency a matter of altogether secondary importance.

The following facts stand in the way of the popularity of the cheques. They have to be drawn up in a set form and a single erasure or mistake would

* The use of cheques is confined to the Presidency Towns and other big commercial centres and European merchants alone make a free use of these cheques and the development of country clearing in the matter of our cheque system will also increase their popularity.

† The cheque is looked upon as a thing so distinctively British as to be called by the late Lord Avebury—" The Union Jack of Commerce "—The cheque has invaded the domain of the bank note and the bill to such an extent that Mr. D. Drummond Fraser says that " the cheque has hurled the note from its pinnacle of power." Before the recent war cheques were always drawn for high figures say—three to five pounds. When the scarcity of silver sent up its price to an unprecedentedly high figure and when the shilling coin became higher in value as bullion than as coin an increasing use of paper currency was made even for such low denominations as crowns, half crowns, ten shillings and other fractions of the pound sterling. Owing to war requirements an increased stamp duty was levied on cheques but the popularity of the cheques was in no way diminished.

lead to its refusal. Many of the Indian Banks insist that the Rs. 25 limit should be adhered to; *i.e.*, cheques below that limit cannot be drawn. This figure is too high for many of the Indian people whose standard of living is very low. The characteristic of the Indian people which has distinguished them from time immemorial is plain living and high thinking. So long as the standard of living is low the payments to be made though they be many, do seldom come up to the required limit. Hence cheques are not increasingly made use of even by the educated people possessing a banking account.

Again they are to be drawn in English and as it is an infinitesimally small part of the population that are in a position to correctly draw it up in the English language the use of the vernacular on the body of the cheque might lead to its greater popularity.* The removal of stamp duty on cheques as in America, or reducing it to a lower figure would be much appreciated by the public and may increase their popularity.†

India is a land of men of small means and of small transactions and too much use cannot be expected out of these cheques. As Hartley Withers says " the extensive use of cheques is possible only in a community which has reached a high stage of economic civilisation and is also blessed with a high

* The introduction of printed cheque books in Tamil, by the Indian Bank, Madras is an innovation which should be copied by the other Indian banks.

† Privilege should be given to draw the cheques for any amount and the present stamp duty of one anna should be reduced to six pies.

level of honesty among its members." In India the stability of government, political security and an efficient administration of justice exist. But a high code of business morality, increasing density of population, mutual acquaintance and better understanding, continuous production, frequent and regular exchange operations and better accessibility of the banks will bring about a better development of the deposit and cheque system.

10. *An Improved Form of Balance Sheet Common to all Banks.*

Another feature common to many of the Indian banking institutions is that they have not realised the tremendous advantages that would accrue to them by the "light" of publicity being thrown on their affairs. If only they exhibit facts and figures concerning their rapid growth much can be done to attract the deposits of the people.* The present balance sheets of our banks are scarcely intelligible to the ordinary reader. They have not adopted a telling balance sheet the figures of which are replete with information.† Unless this is done the outsider will not be attracted to the bank, much less will he care to deposit his savings therein.

* These facts should not be considered in the light of institutional secrets. A systematic publication of them by the advertising department of the banks would enable the people to trust the banker and instead of locking up their funds in unproductive enterprises the people would willingly deposit their money in the banks.

† The balance sheet of the Central Bank of India, published on 31st December, 1923, is up to the mark in this respect and the graph illustrating the yearly progress is to be commended. All other Joint Stock Banks should follow its lead in this matter.

A periodical publication of balance sheets of the type recommended in the chapter on the Indian Joint Stock Banks will contribute much towards the enlightenment of the public as regards the condition of the bank and the valuable searchlight of public criticism can probe deep into the facts and produce much beneficial effect and bring about a substantial improvement in the bank's position.

Again a comparison of the statements of different banks published simultaneously would afford a reliable basis of criticism and these publications serve as an excellent means of self-education for the banks. This mutual criticism of the banks might result in a uniform policy of business management.

So it is highly desirable that all the banks should send in their monthly statements to the Banker's journal that should be started as early as possible. In the absence of that or other in this country. In the absence of that they ought to be printed in the local gazettes. No reform is more desirable than a uniform balance sheet drawn up on identical lines for all banks and this should conform to the type recommended in a previous chapter or it should be arrived at by a common agreement among the banks.

11. *Issuing of Pamphlets to Educate the Customers and Employees.*

Another practice which the Indian Joint Stock Banks have to adopt is the issuing of monthly

Banks is required and the great advantage of this step would be that the Indian banks need not undertake risky and unsafe business. This might seem a counsel of perfection but it is worth attempting.

13. *Banks should have Foreign Branches in Important Monetary Centres.*

It is not only in their own country that the English and German Commercial Banks try to establish their branches but they attempt to establish themselves in the chief monetary centres of the world. Failing to establish a foreign branch, they at least make some working arrangements with foreign banks and get themselves represented in the foreign country. The Lloyd's Bank has established its relations in five thousand important cities in the world. The newly started P. & O. Corporation of the London Money Market has affiliated itself with the Allahabad Bank and has its business established at all the Indian branches of the Allahabad Bank.

Some of our Banks must be international Banks thoroughly organised and do business of an unimpeachable type. Our growing trade with Japan and America is becoming an established fact and foreign branches at Tokio and New York* will not fail to be

* In New York branches in the fullest sense of the word are not allowed. Agencies can however be established and for this a foreign corporation has to pay a licensing fee of 250 dollars annually to the Superintendent of the State Banking Department. It should also satisfy him as regards its financial stability and its powers under its foreign franchise to open an agency. It must make certain returns in accordance with the provision of section 147 of the Banking Law of New York.

advantageous concerns. At least international alliances should be formed.

The advantages of such a policy are many. It is not out of patriotic desire to see India represented in the foreign field that the starting of a foreign branch is recommended. A systematic encouragement can be given by them to treir customers "to get a footing" in the foreign markets. Trade information of a highly practical character can be gathered. It can link domestic with foreign customers and expand India's growing trade and seek a place for marketing her manufactures. They can take up the financing of foreign drafts for exporters at all times. It is true that the Exchange Banks are now doing this business but there should be a systematic policy on the part of the Indian Joint Stock Banks * to help the domestic trader to get into living touch with the foreign market and it is undoubtedly true that " trade follows the bank as much as the flag."

The parent banks can profit by transacting exchange business with the help of their foreign establishments. There is no reason why the Indian Joint Stock Banks should not take up exchange business and finance the domestic trader's foreign drafts. The jealouys of the Exchange Banks would stand in the way but there is no reason why they should resent fair competition with such strong institutions as it would force them to conduct their business on safe and sound lines. Competition

* They should make it a systematic policy on their part to insure stability of foreign exchange transactions by means of forward contracts. The present Exchange Banks do not specialise in this business.

among several banks to do this business means the importers and general public to purchase their drafts at a lower price than formerly.

The clientele of the bank reap ample advantages in transacting the whole of their banking business with one bank. They make international payments or obtain ample credit facilities in the United Kingdom and in the foreign countries. The foreign branch may serve as a good auxiliary through the medium of advertisement and personal invitation to attract deposits. It may obtain much prominence for the parent bank among the foreign banks by whom its foreign exchange is purchased and among the other banks of the world with whom accounts are kept and by whom drafts against its letters of credit are negotiated.

The foreign branch of a bank practically transforms the parent bank into an international banking institution and thereby vastly expands its usefulness and places it in close touch with long established industrial and monetary centres of the world. As our national savings and income expand the foreign branches of the bigger joint stock banks may enable them to place their funds at remunerative rates of interest whenever an opportunity affords itself, in the money markets of the world by the purchase of foreign bills of exchange as an investment or permit them to borrow funds at favourable rates in the money markets of the world, by issuing finance bills. The foreign branch may enable the parent bank to cultivate friendship and comradeship with

the master financiers of London and New York whose opinion as regards Indian financial matters will be of much value to the Indian Banks.

These are some of the advantages of a foreign branch if it is soundly and conservatively managed. America which was so long dead against the branch bank policy has deliberately undertaken the opening of foreign branches to help their customers. The National City Bank of New York has 45 branch banks in its foreign system and is contemplating an expansion of its business in new fields. They have a number of foreign trade experts whose sole business is to furnish the domestic exporter with the information of the state of foreign customers, the nature, extent and volume of their business and lastly the bank finances the foreign drafts of the American exporter. He opens a current account with the bank and turns over all its foreign drafts to this bank for collection by its foreign branches and this sum is credited to the customer's account. He makes an agreement that the bank should accept all the clean drafts drawn upon the bank itself to a certain limit which is determined by the volume of his export trade and thus the domestic trader finances himself for the short period in the most economical manner and this policy has been named the " refinancing by acceptance " and it is by this means the bank encourages the foreign trade business.

It is high time that our banks should learn such methods and expand their field of operations. They should study local conditions carefully. They should secure continual advice and co-operation of men

internal operations of loaning, overdrafts, discounting and aspire to mobilise our monetary resources should not open a foreign branch as it will be a costly luxury to them.

14. *The Duty of the Existing Banks.*

In order that India might be proud of her banking system, the Indian Banks woud have to perform in future a straighforward, upright and legitimate banking business. They should check speculation on the part of the public who occasionally take "flyers" on the stock exchange with the help of the bankers' money. They should keep proper cash reserve, rightly utilise their loanable money in liquid assets and be cautious in the granting of the loans and in the proper selection of reliable and trustworthy clientele. The Banks should take care to weed out numerous weak clients and refuse to run any risk with those who fail to provide additional satisfactory securities when they require additional accommodation. The Banks should rigidly follow the "no risks" system. The Banks should be careful in granting uncovered credit. Too hasty and too prolific concession of credit, long-term credit, neglect of the principle of division of risk and faulty selection of cover, excessive loans, overdrafts, loose and unbusinesslike methods of accounting, excessive borrowings by the banks, investment of banks' funds in securities of a speculative character, charging of usurious rates of interest, unlawful loans, on real estate, excessive loans to officers, clerks, employees of

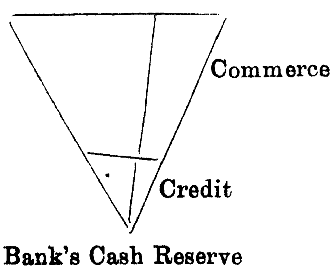
the bank, loans to bank officers or others through "dummies," loaning money directly or indirectly upon the bank's own shares, transactions, of a brokerage or commission business by the banks, executive officers should be scrupulously avoided. So long as the Indian Banks adhere to these golden rules there is no danger as regards their self-preservation but they must take care of their customers also and provide elastic currency which expands and decreases with the ebb and flow of business. They should adapt themselves to the changing needs of their customers. Under the wise direction, legitimate persuasion, helpful intervention, and restraining influence of the Central Bank that is arising in their midst these Indian Banks should successfully function to provide this country with sound and automic currency and such amount of short-term credit as is needed for its commercial, industrial and business requirements. In addition to these the Banks should realise that they are not mere dividend-paying machines. This is but to take a base and mundane view of their function. Unless and until they realise the loftier, nobler and higher conception of banking business, these Banks will not be in a position to fulfil their mission and sacred duty to our country.

15. *The Duty of the People.*

It is neither the individual bank's conservative management nor the watchful guidance of the Imperial Bank that can guarantee the soundness

of our banking structure. Our people should realise that "the modern credit system is an inverted cone resting on an apex of gold" as Lord Avebury puts it. Sir R. Giffen rightly observes "that our credit system is to be likened to the long arm of a lever and the least touch on the cash basis displaces a heavy weight of credit on the opposite end." F. W. Bain who continues Lord Avebury's metaphor says "the cone is a spinning top the point alone on which it spins being of gold, the over-hanging body consisting of paper credit. Confidence is the whipping which keeps the top revolving." A rude shock to public confidence involving the withdrawal of legal tender cash from the banks pulls the top to the ground.

The late Sir Edward Holden illustrated this fundamental truth by the following diagram.



The bottom of the apex is the gold basis of the whole superstructure. A removal of the small portion of gold destroys a large portion of credit which in its turn affects a large portion of commerce carried on with the help of credit granted by the bank.

So our people should have confidence in our banks. Depositors, customers and share-holders should not easily lose their reasoning faculty at the first sign of threatened danger and withdraw their support from the banks.* The Banks should be doing sound business and the customers, depositors, and share-holders should repose perfect trust in them. They should have mutual confidence and this increases consistently with the growth of general prosperity and social sympathy.

The future of banking business in India will depend mainly on tre character of men that will stand at the helm of these leading enterprises. All will be well if these leaders possess the necessary caution. With a more common and better understanding of their business and with a strong sense of solidarity prevailing amongst them they can work wonders and surely achieve thousand times more of what they have attained now.

16. *The Duty of the State.*

The Imperial Bank should be made responsible for the currency and exchange policy of the country. The present policy as outlined by Sir M. Hailey of consulting the Legislative Assembly in all

* Such a lack of confidence was displayed at the beginning of the late war in 1914. Quite recently in March, 1924, there was a run on the Bhawanipur Banking Corporation when it was known that one director had taken a loan of 3½ lakhs of rupees. Our nationalist leader Mr. C. R. Das had to issue a manifesto to calm the minds of the depositors and his communique created confidence with the result that the threatened bank was saved from disaster.

matters of currency and exchange is partly good, partly bad and wholly inefficient. The consulting of non-official opinion is an important step and the criticism that the Government always acts in favour of the L. M. Market interests would not be levelled against it. But it is doubtful whether in intricate matters of currency and exchange, where expert financial opinion has very often gone wrong, the non-official opinion would fare better. Only a few of the members understand technical matters of this nature and to depend on their advice is entirely contrary to the policy adopted by the other enlightened countries.

The currency system should be laid down by an expert Commission and approved by the legislature. After it is once laid down by the legislature, the Government should have nothing to do with it in ordinary times.* In the times of an extraordinary crisis or of a prolonged war when the inflation of currency is an inevitable expedient to finance the war the government treasury would be justified in manipulating it. Even then the aid and co-operation of the Central Bank and the aid and co-operabe enlisted. Almost all civilised countries have left

* Dr. Alfred Marshall says, "the function of a legislature as regards currency is to do as little as possible. Almost any currency of which the position is certain will do its work fairly well. Frequent changes in its basis disturb expectations and infuse a spirit of unrest into business. They may all aim at increased certainty but their effect must on the balance be increased uncertainty. They resemble the frequent wakings of a patient in order to administer sleeping draughts."

the regulation of currency and exchange to the automatic forces of trade expansion and contraction through the mechanism of the banks. Such natural and automatic regulation of currency should be the ideal to be striven for. The Imperial Bank's contribution towards stability should be the cheapening of credit and an effective control over it.

Owing to the fact that the effect of war conditions are still being experienced the British Treasury is still controlling the credit and currency mechanism in co-operation with the Bank of England so that the price level may be stabilised, trade may not suffer as a result of the deflationary policy and the volume and intensity of unemployment may be mitigated to a certain extent, if possible, eliminated altogether.

The next duty which the State has to perform is to appoint a Banking Commission which should tour round the important monetary centres of the world in order to study their banking systems just as the American National Monetary Commission has done. Though its recommendations have not been virtually carried out it has left a mass of literature on the different banking systems of the world which even after the lapse of such a time amply repays perusal. The Banking Commission should examine the present credit situation of the country. It should recommend measures for the organisation of the up-country money markets. It should examine all instruments of evidences of indebtedness in connection with loans and discounts business, bring about uniformity in bills of exchange, acceptances,

bonds, stock and debentures.* This proposal is no new-fangled measure. The Indian Industrial Commission was the first body to make this suggestion. The stress of the war which is always taken as a sufficient plea for the postponement of any effective action has at last been reduced. As soon as the exchange conditions are reduced to their normal state, a Commission should be appointed to study banking, currency and exchange conditions in our country. This Commission should have a permanent existence for a tolerably long period, meeting occasionally to study the effects of its resolutions which are carried out at its suggestion.

The duty of the Commission should be to establisr a banking system which can adapt itself to the expansion and contraction of legal tender as would happen in the event of a commercial crisis. The British banking system perfected itself as it was schooled to a sufficient degree in the adverse days of concurrently recurring crises, and the Bank of England knows its duty clearly at such times. Without the development of a Central Bank the currency policy cannot be shaped so as to benefit the producing classes and cause no loss to the revenues of the Government. The financing of our trade balance should be done through the medium of banking institutions permitting the free movement of bullion and the creation of credit in this country.

* The American Acceptance Councils and the American Bankers are trying their level best to substitute standard forms of employing uniform phraseology for their various forms of credit instruments, instructions and advices.

The Imperial Bank has only to help the Government in the operations of day-to-day finance. Beyond that it should have nothing to do with the Government's financial policy. Now that the Government has balanced its budget and has wisely refused to move down the "slippery slope" of "inflationary finance" the currency and exchange policy can be satisfactorily carried out with the willing co-operation of the Imperial Bank and the other banks. The sooner it is done the better would be the chances for an earlier trade revival in our country.

APPENDIX I

THE PRESIDENCY BANKS.

A Short History.

The present Bank of Bengal * was opened in May, 1806 under the style of "The Bank of Calcutta" with a capital of Rs. 50,00,000 in 500 shares of Rs. 10,000 each. It was granted a charter of incorporation in January, 1809 and the name was altered to "The Bank of Bengal." The East India Company contributed about $\frac{1}{5}$ of the capital but as the bank's capital began to increase the East India Company's proportion of capital began to decrease till in 1876, the year in which the Government sold its shares and relinquished the right of representation on the Board of Directors, the Bank's capital stood at £2,200,000 of which £2,20,000 belonged to the government. The East India Company appointed three Directors and the Secretary and Treasurer of the Bank was always a civilian officer till 1854. It was prohibited to do certain operations by rules in its charter.

A careful comparison of the several provisions in the charter of the Presidency Banks with those

* The origin of the present bank was due to the Accountant-General Henry St. George Tucker's advocacy in the year 1801. He pointed out the inadequacy of the system of floating loans by treasury bills. In order to counteract the influence of local bankers which led to the depreciation of these treasury bills, a bank is to be formed where the government should own a part of the capital. The outcome of this proposal was the present Bank of Bengal. He was the first President of the Board of Directors of the Bank of Bengal.

in the charter of the Bank of England of the year 1695 will lead one to the conclusion that these Indian banking institutions were modelled after that English institution. Like the Bank of England which was prohibited to lend money to the King without the previous consent of the Parliament, the Presidency Bank of Bengal was also prohibited from lending more than one lakh to any individual and five lakhs of Rupees to the Government. The Bank's rate of interest was not to rise higher than 12 per cent. and the Bank of England was also prohibited from raising its rate above 5 per cent. till the year 1839. It was after repealing the usury laws in that year that the Bank of England could discover the effective control exercised by its discount rate in the London Money Market. The Charter also provided that (1) a cash reserve of at least $\frac{1}{3}$ of the outstanding liabilities payable on demand should be kept, (2) the total liabilities of the Bank including deposits, note issues, etc., were not to exceed the bank's capital of 50 lakhs of rupees.

The Charter was renewed in 1823* permitting the bank to issue notes up to 2 crores and the proportion of cash to liabilities was reduced to $\frac{1}{4}$. In 1824 a fraud was practised and the dividend rate fell to $2\frac{1}{2}$ per cent. In 1829 forgeries were conducted by

* In order to meet the growing requirements of trade it was proposed to double the capital but on the advice of the Accountant General, Mr. J. W. Sherer, it was permitted to increase its note issue to four times the capital.

one Raja Kissen Dutt.* From the years 1829-32 the Agency Houses of Calcutta failed and the Bank of Bengal had to experience troublous times and had to break its charter. In the year 1834 the value of the shares fell from 6,000 Rs. to 500 Rs. premium and even to par due to dividend being written off for loans on account of forgeries. But the Bank survived these bad days and gradually began to prosper. Thanks to the vigilance of the Government Directors, the Bank of Bengal did not contract any bad debts during the days of the Great Sepoy Mutiny of 1857. It established branches in Rangoon, Mirjapur, Benares, Patna, and Dacca in 1860, or about that time. The first weekly statement of the Bank of Bengal was published in January, 1856. Owing to the inauguration of government paper currency the Bank of Bengal like its sister institutions of Bombay and Madras lost its privilege of note issue in the year 1862.†

In order to compensate this loss it was arranged that the government should place the whole of its cash balance in the hands of the Bank. Up till the year 1876 the Bank enjoyed the free use of the government balances. From that date onwards the

* The Bank of Bengal lost about 3½ lakhs and the shareholders lost a dividend for one year.

† In 1860 the note issue of the Presidency Banks was as follows :—

Name of the Bank.	Accounts current.	Notes in circulation.
The Bank of Bengal	£ 1,254,875	£ 1,283,946
The Bank of Bombay	£ 438,459	£ 765,234
The Bank of Madras	£ 161,959	£ 192,291

(Bankers Magazine, April, 1893, page 547.)

government undertook to place a part of its cash balances * in the several banks and failing that it agreed to pay interest for the amount of the deficiency. As a matter of fact the balances have been large and there was ample justification for the remark of the Exchange Banks that "the Presidency Banks which are state-subsidised institutions should not be allowed to compete with them in exchange business." Several of the Indian Banks suggested that the government should loan its funds during the busy season on the strength of government securities to all the banks that may be requiring funds. No doubt the ordinary banks † would be forced to do safe business in order to obtain this help but as Sir James Westland has pointed out "the government would be jeopardising its funds by entrusting them to several banks of doubtful standing."

"The Bank of Bengal had to experience another troublous period from 1863-66. As the Bank of Bengal locked up its funds to a great extent it was unable to meet the demands of the government on the public balances it held under its custody. Although half a dozen banks came to ruin the Bank

* *Vide* J. B. Brunyate, Account of the P. Banks, Chapter 7. The original agreements of 1861 were revised in 1866 and these conditions existed till 1876. The average cash balance was to be 70 lakhs at the Bank of Bengal, 40 lakhs at the Bank of Bombay, 25 at the Bank of Madras. By 1876 agreement 100 lakhs had to be deposited with the Bank of Bengal, 50 with the Bank of Bombay, and 30 with the Bank of Madras.

† *Vide* the evidence of the late Mr. Chunilal Saraiya before the Chamberlain Commission, also that of Mr. Vidyasagar Pandya.

of Bengal, thanks to the able management of Mr. G. Dickson, was piloted through the crisis safely.

The year 1876 was an eventful one as the charter of the bank was renewed and an elaborate systematic act applying to all the Presidency Banks was drafted and with some minor amendments in 1879 Act V, 1899 Act XX, 1907 Act I, it still governs the business of the Presidency Banks. Up till the year 1876 the government had a stake in the interests of the Presidency Banks on account of its capital but the government shares were sold and the banks became purely private concerns.

The Bank of Bombay * was started in 1840. Though first projected in 1837 it could not materialise on account of the opposition of large capitalists. Its capital was divided into five thousand two hundred and twenty-five shares of Rs. 1,000 each. The East India Company invested about 3 lakhs as its contribution towards the share capital of the Bank. It nominated three directors and the charter was closely modelled on that of the Bank of Bengal. There were extensive forgeries committed in the years 1848-51 and the Bank of Bombay failed in 1868. Though the bank paid its liabilities in full about 189 lakhs of capital out of a total of 210 lakhs was lost.

The chief cause for the failure of the bank was due to the speculative mania of those days. A

* *Vide* House of Commons Returns 109 and 505 of 1864, or the "Account of the Presidency Banks" by J. B. Brunyate.

commission was appointed to enquire into the causes of its failure. The report attributes the failure to the following causes: (*a*) the Bank Charter Act of 1863 removed many of the restrictions contained in the Act of 1840 and permitted the bank to transact business of an unsafe character, (*b*) the abuse of the powers given by the Act of 1863 by weak and unprincipled secretaries, (*c*) the negligence and incapacity of the directors who omitted to pass byelaws and did not exercise proper supervision over the secretaries, (*d*) the very exceptional nature of the times (speculative mania), (*e*) the absence of sound legal advice and assistance. According to Sir C. Jackson the failure taught the great lesson that "banks should not lend money on promissory notes when all the parties were borrowers and not any of them sureties for others."

The New Bank of Bombay was started in 1870. From 1870-74 it had to experience difficulties. The government could not draw on its balances entrusted to this bank. This together with the incident of 1863 in the case of the Bank of Bengal opened the eyes of the government as to the danger of completely merging their balances with those of the banks. This led to the institution of the Reserve Treasuries at the Presidency towns to hold the balances which were hitherto deposited in the Presidency Banks. The Bank Charter Act of 1876 was made applicable to this bank. The Bank of Bombay began to prosper from that day, thanks mainly to its rigid restrictions.

The Bank of Madras was started in 1843 and received the Charter of Incorporation in the same year. It arose out of the original Government bank which was doing a limited amount of business with a small amount of note issue. The model to be copied was that of the Charter of the Bank of Bengal. The original capital was 30 lakhs of which the East India Company contributed only 3 lakhs. The Bank Charter Act of 1876 was applied to this bank and from that date it had no chequered history as in the case of the other two Presidency Banks. It did good service in popularising banking business in that Presidency.

The Presidency Banks could not play a useful part in the financial system owing to the restrictions under which they were forced to do their business. Some writers have attributed the levying of these restrictions to the jealousy of the East India Company which was doing a considerable amount of banking business, specially the management of the foreign exchange business. Some have attributed it to the goodwill of the East India Company which hoped that these banks as semi-official institutions should be conducted on safe and sound lines. Though these restrictions have gone a great way in stabilising these institutions, they have hindered the progress of the banks and in spite of continuous and unceasing agitation on the part of the Presidency Banks they have not been completely removed. But the ingenuity of the bank officials combined with the customers' need for money helped the banks

to break the actual spirit of the Charter though not its very letter.*

Another feature common to all the three Presidency Banks was their close relationship with the Government and up till 1876 they were quasi-public institutions. The following are some of the noticeable points of contact between the Government and the Presidency Banks. The Government has the right of inspection of the different books and papers of the banks. The balance sheets of the banks have to be published in the local gazette. The Government entrusts its cash balances in those places where these banks have their branches to their safe custody. The Presidency Banks managed the temporary public debts of the Government of India receiving a stipulated payment for it. The government had no intention to keep these banks under its rigid supervision but it secured to itself the right to interfere in case the banks go astray. According to Mr. Keynes " the government is bound to come to the rescue of the Presidency banks in the event of a widespread failure or crisis involving the banks generally, so long as it keeps large balances outside the ordinary banking system and so long as it manages the note issue.† It is the intention of the government that all the other banks should look upon the Presidency Banks as model institutions. The

* *Vide* J. M. Keynes, Indian Currency and Finance, page 202. He instances cases how the Presidency banks virtually loaned money in spite of these rules.

† *Vide* Memorandum on State Bank for India, final report, Chamberlain Commission, p. 60.

relations between the government and the Presidency Banks have been amicable and a systematic policy of keeping a large part of its balances in the banks rendered unnecessary a high bank rate during the period of the late Anglo-German War.*

The Government of India never realised that it is extremely unwise to restrict a growing and expanding business by means of antiquated rules. No doubt they have contributed much towards the solidity of their banking business. Many writers have condemned the retention of these restrictions to the present day. Although exchange has been stabilised by the adoption of the G. E. Standard system yet the P. Banks were not allowed to deal with the business† on the plea that it would be ungenerous to encroach on the vested interests of the Exchange Banks which have done a great deal of service to this country. The Exchange Banks keep their balances with the P. Banks and so the latter should not be allowed to compete with them with the help of their own money. If competition were allowed the exchange banks it is said, would retaliate by combining with some big bank of the London Money Market. So long as the P. Banks have their hands occupied with some business there is not much injustice in disallowing them from dealing with foreign exchange business.

* *Vide* Sir William Meyer, Financial Statement, 1918-18.

† The Bank of Bombay was the first to agitate in the years 1878 to 1880 for the repealing of the 1876 Bank Charter Act in order to permit the P. Banks to deal with foreign exchange business.

Another bone of contention between the government and the P. Banks was the privilege of access to the London Money Market. Although this question was raised in the year 1877 and although the government favoured the proposal of the P. Banks yet the Secretary of State disallowed the measure. His argument for preventing the banks from having access to London were supported by many eminent economists in India. The Hon'ble Mr. H. F. Howard remarked that " the absence of such a thing was not a serious defect but it would be a useful thing." The Hon'ble Mr. T. Smith of Allahabad has thought it " unnecessary and that public opinion would be against it." The late Mr. V. Thackersay and Mr.Chunilal said that "the P.Banks were residuary trustees and hence access should be given to them." Sir Bernard Hunter advocated the proposal " but was against giving the banks the privilege to deal in foreign exchange." Those who object to the P. Banks being granted access to the London Money Market say that (1) " if access were given to them it is not clear it would improve the net aggregate flow of capital into India." To allow them to borrow would be to increase the number of channels through which capital may flow but the volume of it will not increase. But it may be remarked that the exchange banks do not bring enough capital to suit our needs. Hence their access to the London Money Market is desirable. (2) " It would involve the P. Banks to deal in foreign exchange (when remitting the borrowed money) which is a fluctuating thing " but with the advent of the G. E.

Standard system this argument has lost its force. (3) "The money brought in by the exchange banks at least a part of it remains in India in the slack season and is invested in the rupee loans." This improves the rate which the government obtains for them. This would not be the case if the P. Banks were to obtain the funds. But the real grievance is that enough money is not brought over here. (4) "The average rate for council bills will be lowered and during the slack season when money has to be sent back it depresses the exchange." It might be said that the sale of council bills is not to obtain profit but "to meet the present and prospective requirements of the Secretary of State and they must be sold subject to the law of demand and supply." (5) It is quite possible that the banks might not be in a position to pay back the loans for a call for it might be made at any inopportune time. This is the only real objection. (6) State subsidised banks should not be allowed to compete with the Exchange Banks in financing foreign trade. These have rendered meritorious services in the past and the P. Banks ought not to be given undue authority and advantage over these. Whatever their past services might have been, no perpetual monopoly can be tolerated on this score. (7) The three P. Banks competitively pledging government securities is bad and tends to lower the value of the securities.

It is with such reasons that the P. Banks' proposal has been vetoed. But the real necessity for access has not been fully discussed. Evidently the P. Banks wish to have access to the L. M. Market so

that they may borrow money there and remit it to India during the busy season. Owing to the traditional aloofness of the government from the Money Market and its independent treasury system* the evil of the shortage of trade capital is accentuated. As a consequence the banks put up their rates at a high figure and the trading community suffers. Thus there is an acknowledged shortage of trade capital during the busy season.†

The P. Banks propose that they should be given the privilege to borrow funds in the London Money Market but as Mr. Keynes has shown this would not be a true remedy as there would not be sufficient recompensation to the P. Banks if they were to bring over funds from London unless and until they were to be employed all throughout the year at a fairly high rate of interest. This would not be possible during the slack season and hence he has suggested loan's from the cash balances of the paper

* Independent Treasury system resembles a central bank for deposit with branches run by the government in which the government is the only depositor and in which there are no borrowers. Many rupees are swept away from the government coffers just at the time when they would be most helpful in relieving the monetary stringency in the market.

† This feature attracted the notice of Mr. Van Deo Berg so early as in 1884 and he instances the following rates of discounts of the Bank of Bengal as an evidence of the inadequacy of currency for internal commerce.

Year.	Bank rate.	Year.	Bank rate	Year.	Bank rate.	Year.	Bank rate.
1876	$13\frac{1}{2}\%$	1878	$11\frac{1}{2}\%$	1880	$9\frac{1}{2}\%$	1882	$12\frac{1}{2}\%$
1877	$14\frac{1}{2}\%$	1879	$11\frac{1}{2}\%$	1881	$10\frac{1}{2}\%$	1883	$10\frac{1}{2}\%$

(Quoted from Dr. B. R. Ambedkar, The Problem of the Rupee.)

currency reserve. The policy of granting loans is no new thing. As a matter of practice loans were given out of the government cash balances. It defined its loan policy and laid down that "any assistance in relief of the money market which may be afforded by the treasury reserve can be made (1) through the P. Banks (2) at their published rate of discount (3) in relief of temporary stringency." Before 1900, loans were given very rarely. From 1900, they were given on five occasions. Since 1906, there have been no loans. The banks did not care to borrow money in this manner as they were made at the prevailing bank rate and there was no profit for them if they were to relend at the same rate. Had there been any margin the banks would have willingly closed with the offer. Recognising this the Chamberlain Commission advocated the granting of loans to the P. Banks at one per cent. below the prevailing bank rate.

Other methods proposed were to issue notes uncovered by metallic reserves and the abolition of the independent treasury system.* But the government refused to consider either measure.† Till 1920, this archaic, unwise and inefficient method of dealing with the finances of the nation was continued and the Imperial Bank has at last been allowed not only to absorb the treasury reserves but has

* *Vide* India in 1880, by Sir R. Temple, page 469. An interesting history of the episodes of the independent treasury system after 1876 can be obtained in the appendices to the interim report of the Chamberlain Commission, Volume I.

† *Vide* Sir Ch. Wood's Administration of Indian Affairs, page 89.

also been permitted to have access to the L. M. Market. The Government has insisted on the raising of more capital by the banks. It has allowed the expansion of emergency currency during the busy season according to the recommendations of the Sir H. B. Smith Committee.

APPENDIX II.

A Brief Account of the Early Proposals for a Central Bank.

The proposal for the establishing of a great banking institution* which is to be a quasi-public institution can be traced to a very distant date. "It was in November, 1836," says Brunyate in his Account of Presidency Banks, "that a body of merchants interested in the East Indies approached the Court of Directors of the East India Company with the proposal for a great banking establishment for British India." The advantages cited were that "such a bank would facilitate the employment in India of the redundant capital of England, stabilise the monetary system and be of great use for the receipt of revenue and for the remittance to England of the money required for the home charges." This proposal was referred to the Bank of Bengal for consideration and it was of opinion that it was capable of doing the aforesaid business without having recourse to England. Thus ended the proposal and nothing tangible came out of it.

The second mention of such a great banking

* *Vide* Parliamentary Papers relating to Banks published in 1868-70.

establishment was made by Mr. J. Wilson while advocating the establishment of state-managed paper currency in India.* Mr. Samuel Laing, the next finance minister, also viewed the proposal favourably.

The third mention of such an attempt to create a Central Bank was in March, 1867 when the old Bank of Bombay failed and the Bank of Bengal proposed an amalgamation of the three Presidency Banks. The shareholders of the Bank of Bombay negatived the scheme. Mr. G. Dickson originated this scheme and proposed to start the amalgamated bank with a paid-up capital of 5 crores of rupees. The Viceroy condemned the proposal on the ground that the influence of such an institution would overshadow that of the government itself; that such an institution would be difficult to manage and that Madras and Bombay would prefer separate institutions to look after their interests.

From the year 1899-1901 measures for the establishment of a Central Bank were in the air and there was much correspondence on this subject between the Secretary of State for India and the Government of India. This question was keenly

* "Proposals have been made for the purpose of establishing on a large scale and with an adequate capital a national banking establishment capable of gradually embracing the great banking operations in India and of its branches to the interior trading centres as opportunity might offer. There is a growing want for such an institution and a rapidly increasing field for its operations no one can doubt." *Vide* Parliamentary papers relating to paper currency in India—1861.

discussed by many of the witnesses who appeared before the Fowler's Commission. Mr. Alfred Rothschild elaborated a scheme of his own for a state bank to arise out of the three P. Banks. Sir Edward Hambro, one of the members of the Fowler's Commission, wrote a separate memorandum urging the establishment of a Central Bank modelled on the Bank of France—the Secretary of State referred the proposal to the Government of India. But Sir Edward Law negatived the magnificent proposal. According to him "there is under the present condition no real necessity for the foundation of such a bank in the interests of trade and that although the existence of a strong bank with abundant resources would be useful in connection with possible exchange difficulties and would from other points of view be convenient to government, the direct cost of the establishment would be greater than I venture for acceptance. I am convinced that it is unnecessary to establish such a bank for the assistance of trade and unprofitable as regards the provision of assistance in connection with possible exchange difficulties, but still if practical difficulties could be overcome it would be distinctly advisable to establish such a bank so as to relieve the Government of the present heavy responsibilities and to secure the advantages arising from the control of the banking system of the country by a solid powerful central institution. The difficulty of securing a suitable Board of Directors having the necessary leisure to devote to the business is very great. There are practical

difficulties in the way of amalgamation arising out of provincial and personal jealousies.*

The Secretary of State for India thought that the idea of a Central Bank was a good one but that time was inopportune. Hence the proposal was laid aside.

In the year 1911 Lord Crewe invited the late Sir Lionel Abrahams of the India Office to draw up a memorandum on the subject of the Central Bank. According to Sir Lionel "the depositing in this institution of the whole or the part of the money kept under existing conditions in the district and reserve treasuries would place plenty of funds at the disposal of trade and industry. The substitution of the drafts on the London Office of the State Bank for Council Bills, the borrowing power of the Government both in India and England were the other advantages commented on by Sir Lionel. But he considered that "the banks of Madras and Bombay would lose their importance, and that certain technical difficulties between London and India would have to be overcome."† This memorandum was placed before the Chamberlain Commission.

The Chamberlain Commission found it difficult to examine the State or Central Bank proposal owing to the absence of anything in the nature of a

* *Vide* Sir Edward Law's minute on the Central Bank Proposal, January 31, 1901—(papers relating to State Bank printed in 1911 from the Gazette of India, 1899-1901 publications).

† *Vide* Sir Lionel Abraham's memorandum—Appendix No. 14 Interim Report of the Chamberlain Commission.

concrete scheme and even of any general statement as to what was implied by the phrase "State" or "Central Bank." It requested Mr. Keynes and Sir E. Cable to draw a memorandum on this question. With the help of Lord Inchcape Mr. Keynes has drawn an elaborate scheme and this report is more optimistic about the working of the State Bank than Sir Lionel's. Mr. Keynes has pointed out the defects of the existing banking machinery and money market and according to him the best way to strengthen the present position was to have a State Bank. Mr. Keynes stated the numerous objections to the scheme but he disposed them off with easy and effective reasoning. The Chamberlain Commission recommended the appointment of a body of select experts to consider this question. During the period of the war this question was shelved and the Hon'ble Mr. (now Sir) B. N. Sarma's resolution upon the State Bank gave scope for discussion. In place of the State Bank the present Imperial Bank has been created.

APPENDIX III.

Tables showing the Failures of the Indian Joint Stock Banks.

TABLE 1.

Year of Banks' liquidation.	Number of Banks liquidated.	Authorised Capital.	Subscribed Capital.	Paid-up Capital.
		Rs. (00000) omitted.		
1913 ..	*12	274	164	35
1914 ..	4	709	245	109
1915 ...	11	56	7	4
1916 ...	13	230	20	4
1917 ...	9	76	35	25
1918 ...	7	209	4	1
1919 ...	4	52	6	4
1920 ...	3	10	7	7
1921 ...	7	70	5	1
1922 ...	15	...	...	3
Total ...	123	...	...	193

* 1913 (Nov. and Dec.) saw the commencement of the crisis.

Table showing the Important Banking Failures.

Year of Rgn.	Name of the Bank with its Head Office.	Authorised Capital.	Capital Subscribed	Paid-up Capital.	Deposits
		Rs. (00000) omitted.			
1901	The People's Bank of India, Lahore.	35	22	$12\frac{1}{2}$	125
1904	The Amritsar Bank, Lahore.	5	5	$1\frac{1}{2}$	28
1906	The Lahore Bank, Lahore.	5	$4\frac{4}{5}$	1	29
1908	The Doaba Bank, Amritsar.	5	3	Rs. 65,845	9
1911	The Indian Exchange Bank, Amritsar.	5	Rs. 17,310	Rs. 13,410	2
1898	The Bombay Banking Company.	5	2	1	15
1909	The Credit Bank of India, Bombay.	100	50	10	51
1910	The Kathiwar and Ahamadabad Banking Corporation.	100	75	7	23

1914 Bank failures.

1906	The Hindustan Bank, Multan.	10	10	2	10
1906	The Industrial Bank of India, Ludhiana.	5	1	Rs. 54,208	3
1909	The Public Banking and Assurance Co., Multan.	10	Rs. 17,300	Rs. 1,964	...
1911	The Bank of Peshawar, Multan	5	4	1	2
1910	The Popular Bank, Rawalpindi.	50	20	3	18
1911	The Bank of Rajputana, Umbala.	5	2	Rs. 70,501	8
1913	The Solar Bank, Lahore.	100	1	Rs. 8,500	...
1907	The Orient Bank of India, Lahore.	25	10	Rs. 71,354	...

Year of Rgn.	Name of the Bank. with its Head Office.	Authorised Capital.	Capital Subscribed	Paid-up Capital	Deposits
		Rs. (00000) omitted.			
1904	The Punjab Co-Operative Bank, Lahore.	25	10	8	43
1912	The Bank of Asia, Lahore.	25	4	Rs. 32,099	...
1913	The Union Bank of Commerce, Bombay.	50	...	...	...
1913	The Commercial Bank of India, Gazipore.	10	Rs. 5,775	Rs. 4,250	...

1915 BANK FAILURES.

1913	The Amritsar National Banking Corporation.	10	1	1	1
1912	The Standard Bank of Bombay.	20	20	10	...
1912	The Cosmopolitan Bank, Bombay.	20	1	1	...

Explanation of the Tables.

The first lesson to be learnt from these tables is the startling difference between the authorised, subscribed and paid-up capitals. The low proportion of paid-up capital which is roughly 13 per cent. of the authorised capital should be noticed.

The second lesson is that the storm centre was in the Punjab where the banks that arose out of the industrial and swadeshi boom of 1906 came to grief.

The third lesson is that the banks have assumed astounding and misleading titles in many cases.

Both the tables are taken from the Statistical Tables relating to Banks in India, ninth issue.

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EXTRACTS FROM OPINIONS AND REVIEWS.

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"It is an instructive little volume. The author is severely critical of the lack of sound management which has been the cause of the failure of so many Indian native banks. He is also critical of the exchange banks and accuses them of lack of consideration for small accounts in India. He is very hopeful however that India's needs will be met by the new Imperial Bank though his views in this respect are not by any means narrow and he recognises the necessity of co-operation of Indian Banking with the London Money Market."

Calcutta Review—September, 1923.

"The special features of the book are its clearness and lucidity of exposition, comparisons of certain features of banking in India with those of other countries and suggestions for banking reform. The attention of the readers may, however, be particularly drawn to the chapters on the "Indigenous Banker" and "Banking Reform" in which has been presented a mass of interesting information and valuable suggestions.

It must be said that Mr. Rao's book is one of the best books—if not the best book—on the subject of Indian banking and it would prove highly useful to students of Indian Economics who are interested in that subject.

The Lucknow University Journal—February, 1923.

The want of a small handbook on modern Indian Banking was long felt by students of the question as a great difficulty. The present book under review attempts to remove this long-felt difficulty to a great extent. The treatment of Indian Banking by Prof. J. M. Keynes in his classical work on Indian Currency and Finance is much too short occupying, as it does, only one chapter in that book.

Mr. Shirras has no doubt written in much greater detail on the same subject but his book deals not merely with Banking but also with Currency and Exchange problems and these latter topics get more emphasis from Mr. Shirras than Banking. The present book deals with all aspects of the question of Banking in India in a small compass. The author opens by giving a brief account of the Indian Money market and discusses briefly some of the characteristic features of it.

The history of the Presidency Banks, though very brief, is illuminating. In a special chapter the author deals with the exchange banks in India and has given a very lucid account of the intricate and important business of the exchange Banks in India. In particular the author's explanation of the technical banking and commercial terms which puzzle and bore so many readers of the daily papers, will be a real help to the students of Indian Banking in properly understanding this difficult business. The most illuminating chapter is the one on Indian Joint Stock Banks and the author's analysis of the causes which led to the failures of a large number of these Banks, a few years ago, affords a very interesting and instructive reading. The author gives us a chapter on the indigenous banker where he explains the whole organisation of the system of indigenous banking. The recently constituted Imperial Bank of India is treated separately, the reasons which led to its formation and the advantages expected from it, its constitution and methods of business are all lucidly discussed and explained. The author also treats of industrial finance and Industrial Banks, Co-operative Banks and the Post Office Savings Banks.

In the last chapter on Banking Reform the author gives us a very clear account of the lines which our Banking system should be made to proceed and as a result of which it is expected we shall soon succeed in developing a stable

and vigorous system of banking in India—to the lasting good of her country and her people.

On the whole, the book under review is an admirable presentation of a very difficult subject and it bears evidence of much hard and clear thinking. At a time when the development of sound banking is a matter of vital importance in the country the author's book will go a great way in bringing "knowledge without tears" to many people—students and business men alike—on a subject which was long regarded as dry and difficult. We welcome this book as a great aid to our students and we congratulate the young author—who is a lecturer in Banking in the University of Calcutta—on his excellent handbook not merely for the ground that he has covered but also for the scholarship he has displayed.